

INDIAN CURRENCY  
AND  
BANKING PROBLEMS.

TANNAN & SHAH



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# **INDIAN CURRENCY AND BANKING PROBLEMS.**

BY

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INDIAN CURRENCY

AND

BANKING PROBLEMS.

MORHAN LAL TANNAN

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## INTRODUCTION.

The attention which the study of Economics in all its branches is now receiving dates from quite recent times. It is, therefore, more academic than practical in character. The much talked of man in the street has still but the haziest notions about the nature and scope of the science, which, alone perhaps among the liberal sciences, concerns most intimately the everyday life of all human beings. Whether professed economist or not we are all interested and concerned to know why prices fluctuate; incomes rise or fall; taxes are imposed or repealed. But, until quite recently, the men who would be best qualified to analyse and explain these phenomena studiously avoided any attempt which would make them suspected of any leanings towards academic discussion. If the science as a whole is thus treated with indifference, if not contempt, we can hardly expect its more specialised branches to receive greater attention, however closely they touch our ordinary relations in life. It is true, indeed, that certain branches of the economic science did receive a great deal of attention long before the science as such was formulated; and among these branches the place of honour belongs by right and by tradition to finance public as well as private. But the professors of these branches in the bygone times were all practical statesmen and financiers, whose greatness is too well established by now not to admit that they acted most frequently by the "rule of thumb" methods, leaving little room for the broad and well-conceived generalisations of a science. And the traditions of those masters continue to affect the



practical man even to-day. He does, indeed, know in some vague, undefined way that the changes in the currency and banking organisation of the country affects his business; but he knows little, and cares still less, about the nature of those changes, their workings and their consequences, and is, therefore, indifferent, if not sceptic, about the possibility of improvements.

The indifference or scepticism of the average man of affairs is no doubt due in a great measure to his education; but it is also due in part to the general character of the writings of acknowledged authorities on the subject. Owing to their desire to produce a system, a connected whole, the older writers almost always included their remarks on the practical aspects of economics in the one single treatise relating to the whole science. And though of late the tendency is discernible to write monographs on specific subjects—notably in American writers, they still use a phraseology and an imagery reminiscent more of the schoolroom than of the bourse or the counting-house. The result is that the practical business man views with an ill-concealed suspicion the efforts of the academicians to encroach upon what he thinks his own preserves. And so the knowledge of the basic principles of the science of Currency and Banking, as well as its relation to the development of industry and commerce, is not so widely spread as may be desired.

Under these circumstances the production of a book, which deals with particular problems in a simple and intelligible language, would not need any lengthy apology. Besides, the existing literature on

the specific problems of India is of the meagrest. The history of the Indian Currency system in all its branches, and from the earliest time to date has seldom been attempted in a single treatise. There are, no doubt, works of numismatic authorities, such as of V. A. Smith, or Rapson, or Cunningham, dealing with coins and coinage of ancient and classic India; and of Princeps and Thomas dealing with those of India under the Mohammedans. But these are rather attempts to reconstruct the lost political history of India than endeavours to throw much light on the social life and economic organisation of India at different epochs. The point of view being different the net contribution of these writers is necessarily different. They do not claim to give us that account of the development of the currency system of India which would be indispensable for a proper understanding of the present day problems in that subject. Even in the history of India under the British rule the part dealing with currency and banking is sadly neglected. Such material for the subject as we might find in public documents, like Government gazettes or dispatches, or departmental blue-books, or reports and minutes of evidence of special commissions of inquiry, is either inaccessible, incomprehensible or antiquated. The only remaining source of information consists of specialised monographs like those of Prof. J. M. Keynes, of Messrs. Alakh Dhari, Ellstaetter, Kemmerer, Pomeroy Webb and a number of contributions in the periodical press. But we venture to think they, almost all of them, suffer from two cardinal defects. Hardly any one of them attaches sufficient importance to the history of the system, and most of them are avowed champions of the one

or the other side in an open controversy. They are therefore disqualified to give their judgment as unimpassioned scientists. And as to banking, with the exception of Brunyate's and Cook's antiquated works, there is no book dealing adequately—much less exhaustively, with the history and organisation of Banks in India, with suggestions for improving the mode, and increasing the extent, of their business.

The following pages, the authors believe, are a conscientious attempt to avoid either of those defects, though they fear they have not always been able to maintain their ideal. They have ventured in more than one place to take views not accepted in official, and in some cases in non-official quarters. But in every such instance they have done so after a full and exhaustive examination of all the evidence at their disposal. Further, in order not to be misinterpreted or misunderstood, they have, at the risk of appearing presumptuous, made definite suggestions for changes wherever practicable. Altogether they trust the book will not only be a help to the average university student in his prescribed courses of study, but, they flatter themselves, would prove interesting to the business man as well as to the public official.

As to the accuracy of their foresight, in cases where they were obliged to predict, the authors may confidently appeal to the course of events since their manuscript was handed over to the printer. They have argued, for instance for the need of introducing a gold currency with a gold mint and in the last great, historic pronouncement of the Viceroy only a few days ago, the announcement was made that a branch of the Royal Mint would soon be



opened in India. This is not exactly the change the authors would have desired, but still it goes a long way to prove their main contention. It is open to them still to hope that the irresistible logic of facts will at last—after the close of the War—drive the Government of India to adopt frankly and fully a gold currency for India with an open mint for gold coinage. Again, they have argued that the introduction of one or two rupee currency notes would not remedy the present currency situation to any appreciable extent; and, though the Government of India seem to have committed themselves to that step, the authors still find no reason to revise their judgment in that behalf. They wait to see whether the experience of this experiment, when accumulated, would confirm or refute them.

The exchange situation, the authors are aware, still continues to occasion the greatest anxiety. Since they completed the chapter dealing with the effects of the War on the currency system, many steps have been taken to relieve the exchange situation in particular, and to solve the currency problem in general. In the first place the Exchange Banks were instructed to discount those bills preferably drawn against the export of articles wanted for military purposes; and as regards other bills they were required not to discount them unless they got equivalent covers, and later on it was also understood that the covers must be of the same parties. All these steps were taken to render the balance of trade in favour of India as low as possible. Then came the Gold and Silver ordinance the main provisions of which are that no more imports of gold or silver

should in future take place on private account, all such imports, if any, were taken up by the Government and paid for at certain rates. This ordinance seems to have had a double object. In the case of gold the object seems to have been to centralise the imported gold, to be used in the public interest at the discretion of the Government.

Their one attempt in this direction—namely the issue of sovereigns, has not met with the success it deserves, owing to the sovereigns being bought up at a premium from the parties to whom they were issued, by bullion-dealers in great commercial centres. And as regards the prohibition on the import of silver the object seems to have been as much to discourage speculation in silver as to obviate all rivalry from India in the London market against the Government of India. But, as in spite of all these measures, the balance of trade still continues to be in favour of this country, they have as a last measure, since the middle of August last, raised the gold price of the rupee—as far as the councils are concerned—to 1s. 5d. The step has, of course, been violently criticised. Certainly in view of the text of the Ordinance of 1893 the Government's power thus to raise the value of the rupee, once fixed, may be open to doubt. But, we think in the face of the extraordinary situation of to-day Government might well stretch the letter of the ordinance to ease this unexpected situation. Whether it has effectively remedied the situation, whether there have not been some untoward, unwelcome consequences is a question which the authors do not believe this is a fit place to discuss in, even if they had all the material at their disposal to do so.



In the preparation of this work the authors have obtained valuable assistance from the authorities already enumerated in a previous page of this introduction. To single any one of these for special gratitude would cause an invidious distinction, amongst men each eminent in his own way, each entitled to appreciation for his own particular contribution. Besides, the intelligent reader would be able by himself to determine the contribution of the present authors and their indebtedness to other writers on the subject without any assistance of an enlightening paragraph in that behalf from the authors themselves. In this place we need only add an apology—an apology, which, we trust, will not diminish the merits of the work—because it is necessary. The book had to be prepared under great difficulties. In trying to secure the interests of their students, the authors were obliged to use haste, which has, no doubt, prevented that long deliberation and full discussion which would have added immensely to the value of the work. Errors of fact, more harmful than the errors of language, may, therefore, have crept in unperceived in some cases by the writers; and they can only hope that they would correct them all in a new edition, whenever one is required.

We may take this opportunity to express our gratitude to Mr. R. Aitken, of the Bank of Bombay, for his many and valuable suggestions especially in the chapter dealing with the Presidency Banks.

In conclusion a word may be added to explain the specific share of each of the joint authors in the

preparation of this work. For all expressions of opinion or suggestions the authors take the joint and undivided responsibility, as every chapter in the work has been jointly considered before being finally settled. But the chapters dealing with the history and the organisation of the currency system owe more to Prof. K. T. Shah, while those dealing with banks and banking owe more to Mr. M. L. Tannan. Further than this no distinction can be made in the preparation of a work in which each has taken his share, and each has done his best to improve the contribution of the other.

BOMBAY, }  
20th Sept. 1917. }

M. L. TANNAN,  
K. T. SHAH.

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# PART I

## INDIAN CURRENCY.

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### CHAPTER I

#### Indian Coinage.

The history of coinage in India is as interesting as it is ancient. The earliest known Indian coins go back to a date far anterior to the invasion of Alexander of Macedon. Says the Imperial Gazetteer (Vol., II p. 135). "The introduction into India of the use of coins, that is to say, metallic pieces of definite weight, authenticated as currency by marks recognised as a guarantee of value, may be ascribed with much probability to the seventh century B. C., when foreign *maritime* trade seems to have begun." And the writer of this article, Mr. V. A. Smith, goes on to add, "There is reason to believe that the necessities of commerce with foreign merchants were the *immediate* occasion for the adoption by the Indian people of a metallic currency as well as of alphabetical writing." In spite, however, of the deserved-

ly great reputation of Mr. Smith in all matters pertaining to our ancient history, we are constrained to differ from him in this respect. For he seems to assume that a currency would be needed in a civilized country only for the purpose of international commerce. No sooner do the phenomena of exchange make their appearance in any society some form of currency would be needed to affect those exchanges. We may safely assume, that the traditional self sufficiency of India was at least as great in the centuries before Christ as in the centuries that followed; that, therefore, the foreign trade must have held quite a subordinate position in the economic organisation of the ancient Indian society, particularly if we mean by foreign trade trade with countries outside the geographical frontiers of India and conducted by the sea routes; even to day, when foreign commerce has assumed such gigantic proportions in the exchanges of civilized nations, the foreign commerce of the United States has been estimated by President Wilson to be only 4 p. c. of the total trade of that country; that the development of exchange amongst the people of India themselves must have been considerable even in the age of the Ramayana and the Mahabharatta; and that consequently the need for some sort of a currency for the purposes of the internal exchange must have been felt long long before a similar need for facilitating foreign commerce was realised. It is pretty certain that in the age of Manu, whatever its date may be, the art of coinage was under-

stood in India. From the table of weights\* and measures of precious metals, appended below, it would seem as though the people of his day were not unfamiliar with the use of precious metals for monetary purposes. And Manu, to his rationalistic interpreter of to-day, must have recorded only the existing state of things with which he was familiar. According to Mr. James Kennedy † coinage in the eastern countries was the business, not of the state, but of the banker and merchant. Mr. Smith in the article already quoted accepts this theory, and lays down that "the earliest Indian currency was struck by private persons, not by governments." This belief seems to have as slender a foundation as that about the origin of the coinage

**\*Table of weight compiled from Manu VIII § 134.**

SILVER.	GOLD.
2 Ratis=1 Masha.	5 Ratis=1 Masha.
16 Mashas=1 Dharana.	16 Mashas=1 Suvarna.
10 Dharana=1 Satamana.	4 Suvarna=1 Pala or Nishka.
	10 Palas=1 Dharana.

The subjoined tables, collected from different sources, may serve to illustrate more fully the subject of Indian weights.

**Table of Indian weights given by Babar. (Memoirs p. 332).**

8 Ratis=1 Masha.	12 Mashas=1 Tolah.
4 Mashas=1 Tang.	14 Tolas=1 Sir.
5 Mashas=1 Miskal.	40 Sirs=1 Maund.

**Table of weights (Kashmiri) given in Ain-i-Akbari.**

6 Ratis=1 Masha.	16 Mashas=1 Tolah=96 Ratis.
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† (Early Commerce of Babylon with India J. R. A. S. 1898 p. 281.)



of India. We have no means of knowing, and we have no need to dogmatise about, the practice of the most ancient peoples in the earliest antiquities. But, if contemporary evidence can be relied upon, the Indo-Aryans knew quite well the value of the royal prerogative and monopoly of coinage. Chânakya, writing in the 3rd century B. C., gives minute directions for the Master of the Mint, to use a modern phrase, evidencing thereby that already in his day people understood sufficiently all the intricacies of monetary science, including assaying, seigniorage, token coins &c. His remarks on this subject are so very interesting that we make no apology for quoting them here at some length. "The Superintendent of the mint shall carry on the manufacture of silver coins made up of 4 parts of copper and a masha ( $\frac{1}{5}$  ?) of any one of the metals-tikshana (iron or steel), trapu (tin), sisa (lead) and anjana. There shall be a pana, a half-pana, a quarter-pana and an eighth of a pana". According to the commentator these were coins which may be received into the treasury, and, we may take it, therefore, they were full-weight legal tender money. Besides these there were token coins made up of 4 parts silver, 11 parts copper and one part of any other metal. These coins were "a masha, half a masha, a kakani and half a kakani". The author adds "The examiner of coins shall regulate currency both as a medium of exchange (Vyavaharikim) and as legal tender admissible into the treasury (Kosapraveshyam)."



Ancient Indian coins, it seems were bits of metal more or less rectangular in shape, occasionally trimmed at the corner to bring about the required weight. Sometimes the coins were altogether blank, more frequently blank on the reverse only, and still more frequently that side is impressed with one or two small punch marks. The other side has many such marks. The metal is usually impure silver containing about 20 p. c. of alloy. This was prepared as a plate to be cut up into strips from which the coins of the required weight were eventually cut off. Besides these punch marked coins and along with them cast coins, usually of copper or bronze, were also in circulation. In this case the metal was struck with a small die when in a half fused state to produce a square or circular hollow. The most numerous coins of this description have been found in the Punjab, and are ascribed to the great city of Taxila; and they enable us to trace clearly the system of cast coins. Originally they were cast from single dies but soon after the Greek invasion the double die system was generally adopted.

The standard coin according to Chânakya seems to have been the Pana. It is difficult to say what relation that coin would bear to the medieval "tankah" and the modern "rupee;" but the following extracts from recognised numismatic authorities may serve to throw some light. Says Sir W. Elliot, in reply to Mr. Edward Thomas's inquiries\* on the subject, "The currency of the Dekhan seems always

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\* Chronicles of the Pathan Kings of Delhi p. 171 and 224.

to have been gold under the Hindus. The standard was the Hun (in Dravidian Hon, Pon), but the circulation was carried on chiefly by its fractional parts, the *panam* or *fanam*, as is the case in Travankore, the only existing normal Hindu State to-day. There the dealings of the bazaar and the collection of the revenue are all made in fanam, but as the labour and trouble of reckoning large sums in such a shape would be intolerable, the cashiers and sarafs are provided with wooden boards, the surface of which is studded with 100 or 1000 cavities, the exact size of a *fanam*, which they plunge into the heap of coin, and by a little manual dexterity, take up the exact sum and throw it aside. In early times, not only the *fanam*, but half and quarter *fanam* were in use. I have specimens of all these bearing the impress of the Chalukya Boar, the Pandyan fish and other effigies of date far anterior to the star pagoda." The same authority elsewhere says, "The Gunja or unit ( $= \frac{1}{4}$  fanam) is the Rati or Sanscrit Raktika, the seed of the abrus. I have weighed numbers of these and found them to vary between  $1\frac{1}{2}$  to 2 grains, or even more; a fair average would be  $1\frac{3}{4}$  grains. On this authority the average weight of a gold panam would be 6 grains, that of a half-panam 3 grains, and of a quarter panam  $1\frac{1}{2}$  grain." In other words this panam would be  $1/30$  of the weight of the modern rupee, and if we take the present ratio of silver and gold to be 30 : 1 the *panam* would be equal to 1 modern rupee in value.\*

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\* A पण is a particular coin=80 cowries V. S. Apte's Sanscrit Dictionary.

It may indeed be doubted whether the identification between the *panam* or *fanam* or *hona* with पण of Chánakaya has any sound basis in the history of the period, since the oldest available coins are of silver or of copper or bronze as mentioned above rather than of gold as such an analogy or identity would suggest. The explanation may be that the true Indian Currency has been preserved and continued more by the peoples of the southern peninsula than by those of the northern plains who were so easily susceptible to external influences.

Whatever be the material and the present day equivalent in value of these *Panas*, it seems that there must have been bigger or other coins to make large payments. There were the *Suvarnas* of approximately 145 grains or 80 ratis equal, at the modern rate of exchange, to 18 rupees in silver. These *suvarnas* were debased by Skandagupta. On the other hand it is on record that Ambhi, King of Taxila, paid Alexander the Great 80 talents of coined silver. These were only stamped, flat pieces of silver, square or oblong in shape, and of considerable weight. According to Rapson this kind of coinage was used throughout ancient India. The coins found in the Punjab have inscriptions upon them both in the Greek and in the Brahmi tongues; and though they represent considerable advance on the earliest known Indian coins, they still have the same square or oblong shape. The oldest known coin of ancient India, which is not punch marked

but struck off a single die, is of bronze and of the days of the Maurya Emperors of India. It is also the first circular coin that has come to us from ancient India.

There were also gold coins in circulation in ancient India. It seems to have been the characteristic of Indian trade for ages past that the exports invariably exceeded the imports. The balance has had, therefore, to be paid in precious metals. And so in several parts of the country, and particularly in the Deccan, with its considerable sea-board and the consequent maritime commerce, we find foreign gold coins, principally the Roman *aurei*. The Punjab, too, though inaccessible from the sea, has preserved a number of similar coins; but perhaps the explanation in this case may be that the Indo-Greek kings of Bactria, acknowledging, however faintly, the supremacy of the Roman Eagle, were wont to show this mark of respect to the distant suzerain by the easy and obvious device of imitation of the coinage.

It would take us far beyond the bounds of this modest work if we were to attempt, however briefly, a history of Indian coinage from the earliest times. Suffice it to say that the early Indo-Aryans had reached a very high degree of excellence in applying the principles of monetary science; that they knew all the mysteries of legal tender and the intricacies of standard and token coinage; that they appreciated the importance of seigniorage and were familiar with



the devices of counter-feiters. One emperor, Skandagupta, had even to resort to the doubtful expedient of a debasement in currency in order to remedy the financial distress of his administration. At the time of the Mohammedan conquest the different kings of India had their own coinage of gold or silver, conforming as far as possible, to the ancient standard prescribed by Manu and Chanakya and Varahamihira. They each regarded—and justly so—coinage as a royal monopoly and endeavoured successfully to guarantee the weight and fineness of their coins. As regards the mere technique of coinage, the design and shape of their coins were not all that could be desired, though even there, considering the then state of metallurgy, they had attained considerable excellence. Gold and silver being current side by side we may presume they had a sort of practical bimetallism; and though we cannot say what precisely was the ratio of exchange between the two metals, the weight of authority inclines to the view that the pre-Mohammedan ratio was 8 : 1 between silver and gold.

### **Indian coinage under the Mohammedans.**

When the Mohammedans first entered India they seem to have struck coins of both gold and silver to some extent ; but for the general purposes of every day life the first conquerors maintained, almost intact, the local currencies as they found them. The right of coinage, together with the mention of the

ruler's name in the public prayers, was regarded among the Mohammedans as the indispensable mark of independent, undisputed sovereignty, and consequently Shahab-ud-din Ghori and his immediate successors upto the time of Altamash did, indeed, strike some coins. But the purpose of these coins seems to have been rather the commemoration of a victory or any other public event of the kind, than to serve as currency. The existing coins of the period, with their inscriptions in Nagri characters, and having on their face names of local rulers along with that of their conqueror, bear out the same supposition.

There was also another reason why the first Mohammedan kings of Delhi could not issue their own coins for any considerable currency purposes. Being slaves by origin, they were under a peculiar necessity to suppress their ultimate grandeur. To strike their own coins would have been an overt act of treason, which could have been easily brought to the notice of their nominal masters in Ghazni by the itinerant fakirs. After the disappearance of the strong hand of Shahab-ud-din, Kutb-ud-din, it is true, might have struck his own coins to give visible proof of his viceroyalty having been transformed into an independent royalty; but just then the kings of Delhi were suffering from a shortage of bullion. One reason of that shortage may be the removal of vast stores of the precious metal by Mohamud Ghazni and his successors in the path of looting India. Hence even if they had wished it they

could not afford to issue any extensive currency of gold or silver from their mints. We may take it, then, that beyond a few pieces of medal, struck rather to gratify royal vanity than to minister to the needs of commerce, the first Musulman kings of Delhi did not venture on any considerable coinage enterprize. An examination of the extant coins of the period shows that the ordinary currency consisted of the coins of the conquered princes, with modifications introduced to show the political transformation which India had undergone. The inscriptions are Hindi at the beginning, to be converted into Arabic, after a short interval during which they were bilingual. The figures were, on the obverse, either of the Goddess Laxmi or an Indian horseman, and the names, on the reverse, those of local rulers, either by themselves or in company with that of the reigning emperor at Delhi. The exact weight of these coins we do not know ; but the largest gold piece had been found to weigh 93 grains and is circular in shape while the corresponding silver piece weighs 133 grains.

When the reasons of prudence or necessity were no longer existing to restrain the successors of Kutb-ud-din from instituting a local coinage of their own, they cast about for means to issue a legitimate currency. We may date the beginning of the Mohammedan coinage in India from the 23rd day of the first month of 626 A. H., corresponding roughly to 1227 A. D., some 30

years after the establishment of the Muslim Empire in Delhi. In that year Altamash was officially recognised and confirmed as an independent Sultan by the Caliph, the head of the Muslim world. The first coins struck on this occasion bear evidence of the enhanced dignity of the Indian ruler; and all authorities are now agreed that the coins which followed—the so-called Delhiwals—were all fashioned after the model of the coin struck on that occasion. The money of account with which the later generations of Indians were so familiar—the immemorial “Tankah” \*—is thought by some to date from that day. Contemporary writers, like Hasan Nizami, the talented author of *Taj-ul-Masir*, refer their money values from this time onward to Delhiwals; and though they speak of Dinars and Dirhems also, these were probably coins, not turned out by the Indian Mints, but rather of the countries from which the writers—or the rulers—hailed. No doubt these coins too were current in India, for their mention suggests that they were in general use. In fact we find mention of the Dinars and Nishka even in the

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\* Historians are not agreed as to the origin or derivation of the term ‘tankah.’ Erskine, (*History of India* Vol. 1. p. 456 ) says it is derived from the Chagatai Turkish word for white viz. “Tang.” This, however, seems rather an unnecessary display of scholarship or imagination—since the word, as Wilson says, was used for coin in general, and was regarded in the country as equivalent to a given weight of silver i. e. 4 Mashas. The word is found in almost all the vernaculars of India from very early times.



works of the immortal Bana Bhat who flourished under the Emperor Harsha in the 8th century of the Christian era. But such a mention in no way makes the coin an indigenous Indian coin ; it only suggests the extent of Arab influence in India four centuries before they finally conquered her. From this date onward we may take it, the standard Indian coin is the Delhiwal-or the tankah-of 168 to 180 grains in weight-and taking its name from the city where it was originally minted.

Altamsh, therefore, may be regarded as the author of the standard Indian currency of silver. The standard, its weight and fineness, as fixed by him remained unchanged for a period of 90 years. He coined gold, too, a little later, and these gold coins were based on the model of the tankah, being of the same weight, design, and shape, but not of the same size. The bulk of the currency consisted of bilon\* money, with the subordinate copper pieces which the Mahommedans received from their Hindu predecessors. Altamsh, however, issued a considerable amount of small change from his own mint, so that as Farishta says, " In order to comprehend the true value of the money of that date it is proper to state that a Tankah ( the standard coin ) was a tolah in weight whether of gold or silver, and a tankah of

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\* " Billon is an alloy of copper and silver mingled in irregular and widely varying proportions. " ( Imperial Gazetteer, Vol. II, p 144 ).

silver was equal to 50 jitals. The "Jital" † he adds, "was a small copper coin the weight of which is not now known. Some conceive it was a tolah, while others are of opinion that the Jital like the pice of the present day, weighed about  $\frac{7}{12}$  of a tola pice." (Trans...by Briggs Vol. 1. p. 360.).

This standard, as established by Altamsh, continued unaltered upto the time of Alaud-din Khilji. This unscrupulous ruler, having an unduly large army, essayed to support it by debasing the coinage. He reduced the weight of the standard Tankah from 180 grains to 140; and that the reduced weight might not affect prices, he tried to fix the prices of commodities by a royal decree in such a way that the soldier could purchase for the same number of the new coins as much provisions as by the old coins. The Adali—as the new Tankah of 140 grains soon came to be known, proved unpopular, and even the absolute autocrat of Delhi had to acknowledge this natural law of monetary science. The debased coins did, indeed, remain in circulation for a time, but at a value conforming to the intrinsic value of silver in the coin; and so we may say that the changes of Alà-ud-din were short-lived.

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† It may be remarked, in passing that the Mint authorities in India maintained the same excellence under the Mohommedans, that they had reached under the Hindus. Though some of Altamsh's earlier coins were imperfect from our modern standpoint, the coins of his successors, both of gold and silver, show a high degree of finish and artistic value. Indeed, if we make an allowance for the state of the metallurgical science of the times, they seem to have aimed at absolute perfection.

The next important name in the history of Indian coinage and currency is that of Mahomed Taghlak. That able but eccentric monarch seems to have been an honest and far-sighted reformer of the currency of his day, his only misfortune being that he was five centuries ahead of his times. Though local and contemporary writers do not furnish us with any connected account or reliable scheme of the relative value of local coins, we have ample material to determine, approximately, the changes made by Mahomed bin Taghlak. Two foreign travellers in India, Ibn Batutah of Egypt and Shaikh Mubarak bin Mahomed Anbati, have left us good contemporary accounts, by the aid of which we can piece out the details, and present a connected, consistent story of the currency changes of this 14th century reformer. At the outset we may give the following table to show the component parts of the currency under Mahomed and their relative values:—

- |             |  |                   |                    |
|-------------|--|-------------------|--------------------|
| 1 Kani=     | 1 Jital                                    | =                 | 1 pice.            |
| 2 Kanis=    | 1 Sultani.                                 | =                 | (half anna piece.) |
| 3 Sultanis= | 1 Sashkani.                                |                   |                    |
| 4 Sultanis= | 1 Ashtakani=                               | (two anna piece). |                    |
| 64 Kanis=   | 1 Tankah of 175 grains pure silver         |                   |                    |
|             |  | =                 | Rupee.             |
| ‡ Kani=     | 1 Copper fal (damri) <i>i. e.</i> 1 Tankah |                   |                    |
|             |  | =                 | 256 fals..         |

Let us remark in passing the essentially Indian scheme of division as revealed by this table. Arabia and other western countries seem to have adopted long before this time the decimal system, and so with them the division by fives and tens was quite common. With us in India from the earliest time the quaternary scale seems to have been predominant, and the division was rather by fours, sixteens, sixty-fours &c. The table, therefore, proves that Indian scheme of currency organisation had borrowed nothing beyond the inscriptions from the Arabic conquerors, while the latter on the other hand, some centuries after their establishment, maintained the local scheme. Upto the time of Altamsh they maintained the local standard with its local subdivisions ; and it was not until Alaud-din Khilji at first, and Mahomed Taghlak later on had gained different views regarding currency organisation, that changes were proposed partially incorporating the decimal system.

Mahomed Taghlak developed the Adali of his Khilji predecessor and at the same time introduced a new gold piece of slightly higher weight than the old gold tankah of 175 grains. This last was a coin of 200 grains and was named Dinar on its surface. It seems to have enjoyed a very brief popularity judging from the extant specimens which all belong to the years 725, 726 and 727 A. H. Mahomed also altered the design of the old tankah making it more elegant, and executing it with greater accuracy. The new pieces both of gold and silver caused all



the confusion that ensue. Mahomed Taghlak, though a great name in the history of Indian currency, does not seem to have had a clear conception of what we now call standard of currency. In the absence of a definite standard the relative values of gold and silver were necessarily left to be adjusted by the ordinary law of supply and demand, thereby causing considerable confusion not only in the currency itself, but in the level of prices in general. In the days we are now speaking of, the money most ordinarily in use was that of copper, though silver seems to have been the theoretical-the official-standard. Akbar, nearly three centuries after Mahomed Taghlak, when the conceptions of monetary science were more fully realised, accepted the Dam-a copper piece of money-as the unit of all monetary computations. Next to copper silver was the most fixed in value; while gold, both from its relative scarcity and from the desire of the people to hoard it or turn it into ornaments, was peculiarly liable to wide fluctuations. We cannot, therefore, take the ratio between gold and silver as fixed even for a single reign. The margin is wide enough to permit the several figures given by the local writers to be all correct at one time or another, though the most frequent ratio seems to have varied between 1 : 8 and 1 : 10. It must be remembered that, though there is evidence to show that in the time of the Taghlak reformer 10 silver pieces exchanged for one of gold, that does not suggest the ratio of 10 : 1; for if the 10 pieces totalled 1400 grains of silver,

and exchanged for a piece of 200 grains of gold, the ratio would rather be 7 : 1. This is quite probable under Mahomed Taghlak, who abandoned the idea of equality of weight between the silver and gold coins—as was the case uptil his day, and who had, as already noticed, developed the 140 grains silver piece and 200 grains gold piece.

The reasons why Mohomed issued the new gold coins, in spite of all their probable confusion which a man like him must have foreseen, are not difficult to conjecture. Large quantities of gold had been poured into the Delhi treasuries by the conquests and plunder of Alaud-din and Kafur in the Deccan. The currency under the Tughlaqs needed an expansion; and Mahomed tried to give this much needed expansion by the issue of new and heavier gold coins. He did not, however, change the standard which remained silver; the addition of gold coins, therefore served only to cause a confusion and to reduce the ratio between silver and gold to 7 : 1. Confusion, both in the general currency organisation and in the prices, was inevitable, since old pieces were not called in, the new ones were not standardized and no royal firman was issued to regulate prices.

Shir Shah, the last great Pathan King of Delhi, the predecessor and model for many of the great achievements of Akbar, is the next great name in the history of Indian coinage. He introduced a number

of specific reforms in the organisation of the mint, too technical to be sketched in this book but sufficiently important to be copied by his great successor in one form or another as shown by the *Ain-i-Akbari*. He corrected the progressive deterioration of the coinage, brought about by the preceding kings, by discontinuing the time-honoured mixture of metals for the standard coins—which were liable to be so easily debased by unscrupulous rulers or careless workmen of the mints and substituted instead simpler metals. He remodelled the coins and reduced and readjusted the relative values of the lower metals of silver and copper. We have not evidence enough to declare that he fixed even the ratio between silver and gold; but the fact that not half-a-century after his death Akbar accepted and established the ratio of 9·4:1 would go far to show that Shir Shah's reforms must have contributed to the improvement in the value of gold in terms of silver.

With a brief sketch of the system established by Akbar, the greatest of the Mohammedan rulers of India in every department of administration, we may close this section of our subject. Perhaps the easiest way to picture the state of coinage under the great Mughal is to give a simple description of the various coins current. These were:

1. The Shenshahi Mohur : of  $\frac{1}{4}$  101 tolahs, 9 mashas, 7 ratis = 100 Lal Jalali Mohurs at Rs. 10 each.

2. A smaller variety of the Shenshahi weighing 91 tolahs and 8 mashas and equal to 100 round mohurs at Rs. 9. each,
3. Rahas= $\frac{1}{2}$  of No. 1 or 2 according to their contents.
4. Atmah= $\frac{1}{4}$  of No. 1.
5. Binsat= $\frac{1}{5}$  of No. 1 and there were similar coins= $\frac{1}{8}$ ,  $\frac{1}{10}$ ,  $\frac{1}{20}$ , and  $\frac{1}{25}$  of No. 1.
6. Chahar Goshah ( 4 sides ) weighing 3 tolahs &  $5\frac{1}{4}$  ratis=Rs. 30.
7. Chugal weighing 2 Tolahs and Mashas=3 round Mohurs at Rs. 9 each.
8. Ilahi weighing 1 tolah, 2 mashas,  $4\frac{3}{4}$  ratis=Rs. 12.
9. Aftabi weighing 12 mashas,  $1\frac{3}{4}$  ratis =Rs. 10.
10. Lal Jalali\* weighing 1 tolah and  $1\frac{3}{4}$  ratis =Rs. 10.  
=400 dams.
11. Adal Gutka of 11 Mashas, also known as the round Mohur=Rs. 9.

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\* The extra weight beyond that allowed in No. 9 was probably due to the lower degree of the fineness of gold used for these coins.



These coins were all of gold. Besides there were silver coins, viz :—

1. Rupee ( round ) of 11 Mashas 4 Ratis.

2. Jalalah ( square )                   "                   "

with their subdivisions of  $\frac{1}{2}$  or Darb,  $\frac{1}{4}$  or Charu,  $\frac{1}{8}$  or Pandu,  $\frac{1}{16}$  or Ashta,  $\frac{1}{32}$  or Dasha,  $\frac{1}{64}$  or Kala and  $\frac{1}{128}$  or Suki. The rupee was valued at 40 dams.

There were also the copper coins of a Dam, which had come to be regarded as the unit or standard in all exchange, and was the form of ready money of prince and peasant alike, and which was valued at 40 per rupee; the adhela, the pawla and the damri or the  $\frac{1}{2}$  Dam,  $\frac{1}{4}$  Dam and  $\frac{1}{8}$  Dam respectively.

Two points in the tables given above merit more than a passing notice. ( 1 ) The larger coins, of Shenshahi &c. may have been rather medals probably struck to commemorate a special occasion than ordinary coins of every day use. Against this supposition we must remember that there was always a number of such coins in the Imperial Treasury—estimated at 20000 by Hawkins in the days of Jehangir and that the successors of Akbar went on coining them. Perhaps they were designed as a more convenient substitute for metallic money of smaller denomination to facilitate large payments, something like a modern bank-note which might comprise Rs. 10000 in a piece of paper barely 8 inches long and 5 inches wide and 30 grs. in

weight. In Akbar's day, with the less developed credit, a Shahenshahi Mohur may have been meant for the same purpose. Besides, on each of these coins turned out by the Imperial Mint the Emperor got a seigniorage of  $5\frac{1}{2}$  per cent, which may have been a sufficiently tempting reason to put them into circulation.

The other point relates to the increased importance of the copper Dams. The values of all others coins are given in terms of the Dam, and the estimate of the Imperial revenue and expenditure are also made in the same coins. This suggests that the Dam was under Akbar, if not the standard, at least the unit of currency, and it remained so for a long time under his successors.

After fixing the weights and relative values of the different coins, Akbar had next to determine the ratio between silver and gold. Under his predecessors—Hindus and Mahomedans—it had fluctuated between 8:1 and 10:1; and under the Tughlaqs it had probably fallen as low as 7:1. The value of gold, however, was appreciating, and Akbar fixed officially the ratio at 9:4:1.

With the elaborate regulations of coinage that Akbar introduced or amplified, he also found necessary to lay down a detailed scheme of mint royalties or seigniorage. The sub-joined table gives a clear conception of the well-recognised law of state seigniorage—which works out at over  $6\frac{1}{2}$  p. c. for turning bullion into coin.

Outlay by merchants in current coin, for crude metals.	Total mint return after re- * fining.		Merchant's re- turn, with frac- tional profits.		State seigniorage.		Mint Charges,	
	M.	Rs. D. J.	M.	Rs. D. J.	M.	Rs. D. J.	Rs.	D. J.
100 Lal Jalali gold mohurs.	a.	105 39 25 0	100	12 37 3½	5	12 3½ 0	7	26 20½
Rs. 950 (crude metal test).	b.	1006 27 20		953-21-10½		50 13 0	2	33 2
Rs. 950 (old coin test).	c.	1015 20 0		954 29 0		50 24 0	10	12 14½
1044 Dams= cost of 1 man copper.	d.	1170 0		1062 19½		58 20	1	8 18

\* In this table M=Mohur, Rs=Rupees, D=Dams, J=Jitals.

NOTE:—There are obvious discrepancies in the totals of the three last columns as compared with the first. We have, however, simply reproduced the table from Mr. Thomas, who himself has noticed the error, but who makes no effort to correct it.

The system as elaborated and established by Akbar Shah was maintained in all its essentials by his successors. As the outlying parts of the Peninsula were conquered by the Mughals and incorporated into their empire, the whole of the Indian continent came at last to have one uniform currency. Previous to the consolidation of the empire under the Mughals, the whole of India perhaps never had a uniform currency, not even under Chandragupta and Asoka, the Maurya fore-runners of Shir Shah and Akbar. For this reason we have omitted all reference to provincial currencies, and confined ourselves to the Delhi currency exclusively, not with any view to deny the importance of the local currencies, but rather in the desire to avoid complications and confusion. We might, however, insert at this stage a brief note on the prevalent Deccan currency in the pre-Mughal days, partly because the Deccan has somehow always managed to retain its individuality as distinct from the Northern provinces, and partly because the currency traditions of the Deccan influenced materially the policy of the English successors of the Mughals. We have already quoted Sir Walter Elliot as saying that the currency of the Deccan consisted of gold under the Hindus. The standard coin was the hun-or hona, but circulation chiefly consisted of its fractional parts the panam or fanam. The invasion of the northern barbarians began to drain the Deccan of its gold; and, though the star pagodas remained in circulation as late as the 18th century, the



rupee\* came to be the standard coin of the Deccan after the establishment of the Mughal supremacy. The adoption of the rupee as a standard by the Mahrattas, completed the chain, and we have ever since the rupee the predominant standard coin throughout India.

With the disintegration of the Mughal Empire, the outward designation of the currency remained unchanged. The different Indian powers set up their own independent mints and struck their own coins. With such a variety in the coining authorities we cannot of course look for uniformity of weight or standard. It would, therefore, be well-nigh impossible to trace the history of the Indian coinage with its vicissitudes from the death of Aurangzeb in 1707 to the establishment once more, on a uniform basis, of the East India Company's rupee in 1835. The task, even if we were able to accomplish it, would be beyond the scope of

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\* The derivation of the term Rupee is not quite certain, though the attempts at it are not without interest. Some have traced it from "Rupyam" from the Sanscrit Rupa—shape of figure, having reference to the effigies on the coin. It is improbable that the iconoclast Mohomedans would have adopted—as they did—the term if they had known of such a derivation. A more probable—or at least a more uniformly acceptable origin is from the Sanscrit Rupyam—silver. We do not know when exactly the term Rupaiya began to take the place of the older term tankah, but it is almost certain that it is not earlier than the days of Shir Shah. The Moghuls accepted this designation of the standard coin, extended its use and hence the present name. Mr. Edward Thomas traces the term in reference to its weight to the Sanscrit Shata raktika of 100 ratis or 179 grains.

the present treatise. Suffice it to say here that before the reforms of 1835 came into circulation coins both of gold and silver were generally accepted in India. The East India Company obtained from the Moghul emperors the right of coining in their own mints in 1717 at Bombay, 1742 at Madras, and 1757 at Calcutta. Before these dates the Company did, under the Royal charters, turn out some coins of their own. But henceforward they coined at their Presidency mints the Mughal coins in all essential particulars.

There were 3 principal kinds of rupees in circulation, the Sikkah rupee of the Moghul emperors in Bengal and the Northern Provinces or Hindustan, the Surat rupee of Bombay, and the Arkot rupees in Madras. From 1773 the Sikkah rupee of Bengal had an inscription, 19 San Sikkah, that is to say, coined in the 19th year of Shah Alam. This coin consisted of the gross weight of about 180 grains and with about 176 grains of fine silver. With slight changes it remained in circulation upto 1836. Since January 1, 1838, the Sikkah rupee has not been legal means of payment. The old Bombay\* rupee was somewhat lighter than the Sikkah rupee though it had more fine silver. Under the administration of the Nawab of Surat and of the

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\* The earliest known coins of the Bombay Mint are the 4 Rupees in the British Empire of 1675, 1677, 1678 and 1768. The first has the stamp on the reverse of the arms of the Old East India Company and the remaining 3 have the arms of England.

Bombay Government the Sikkah coin was discontinued. The Surat rupee weighed  $178\frac{3}{4}$  grains and contained  $1\cdot24\%$  alloy. By an agreement with the Nawab of Surat the rupee both of Bombay and Surat was to circulate throughout the territories of both parties at an equal value and both parties pledged themselves to maintain the coin at this standard. The Nawab's rupees, however, soon came to contain  $10\%$ ,  $12\%$  or even  $15\%$  of alloy. As a result Bombay rupees were carried to Surat to be recoinced, and the Bombay Mint ceased to coin silver for more than 20 years, the only coin in circulation being the debased Surat rupee. In 1800 the Government of Bombay ordered the Surat rupee to be struck in the Bombay Mint and from that date the rupee was maintained at an equal value in the Bombay territories. It weighed 179 grains and contained  $7\cdot97\%$  alloy. The Arkot rupee before 1818, struck at the the Mint of Fort St. George, contained 166·477 grains of fine silver. As gold was valued too highly in comparison with silver, the silver rupee had but little importance in comparison with the gold pagoda. It was a small Indian coin rated higher than the British rupee.

In 1806 the Court of Directors determined upon a single silver standard for the East and ordered that the current coin of Madras should be a silver coin of a weight of 180 grains  $11/12$  fine. 350 such rupees were equal to 100 Pagodas. But these new coins were not issued upto January 7, 1818. As the decree would show the Company intended early in 1806 to

issue a uniform coin in their Asiatic possessions. They had, however, to wait 30 years before this design could be carried out. It was only by the Act of 1835 that a uniform silver rupee and the corresponding pieces of  $\frac{1}{2}$  rupee were introduced throughout all India as the legal means of payment. The type chosen for the Company's new rupee was that of Madras as it was issued in 1818 containing 180 grains gross weight and 165 grains of fine silver. Since 1862 the rupee has ceased to contain the escutcheon of the East India Company, and instead has been provided with the effigy of the reigning English sovereign with the name on the coin and the year of its mintage on the back.

#### GOLD COINS BEFORE 1835.

Like the silver rupee the gold mohur of the Mughals had the same old weight of 100 ratis or 175 grains fine gold. After 1785 the East India Company tried to introduce a single gold standard in India ; but the attempt was frustrated, as the gold mohur was not adopted as the legal means of payments in public and private obligations, nor was the ratio between the rupee and the gold mohur quite stable. The mohur, though coined, was very seldom struck ; and its market price was subject to fluctuations, silver being the common standard of value throughout the country.

By the Act of 1835 it was said " no gold coin shall hence-forth be a legal means of payment in any of the possessions of the East India Company".



The gold coin of Southern India was the native Varaha ( Vishnu's boar ) or Hun as the later Moham-medans called it. Before 1818 the current gold coin in Madras was a Star Pagoda, so called from its device. It contained 42.048 grains of fine gold, and was valued at 7sh. 5 $\frac{1}{3}$  d. By a Proclamation of January 7, 1818, the new silver rupee was introduced as a legal means of payments in the Presidency and the coinage of Pagodas was stopped. In 1820 the minting of gold coins was restricted and their legal tender power was likewise limited.

Since 1835 when the single silver standard was adopted by the East India Company, attempts have been made to introduce gold in the Indian coinage system. On January 30, 1841, a Proclamation was made by which the public treasuries were instructed to receive gold mohurs for Rs. 15 and thus the gold mohur became a legal payment at the treasury. No gold, however, was coined, and though the profit of seigniorage was very little, in 1845 hardly any gold was in circulation. About the middle of the last century came the Australian and California gold discoveries. The price of gold fell as a consequence; and so by an ordinance of December 22, 1852, the right to pay gold at the treasury was withdrawn from January 1, 1853. Ten years later during the cotton famine the importation of precious metals into India was enormous and the chambers of Commerce of Bombay and Madras once more agitated for introducing the gold standard. In consequence

on November 23, 1864 the public treasuries were instructed to receive English sovereigns at the rate of Rs. 10 and half sovereigns at Rs. 5. respectively, and tender.

Another result of this agitation for the introduction of gold was the appointment of the Mansfield Commission which reported on October 4, 1866 on the monetary system of India. The use of gold as the legal means of payment was recommended, reckoning 1 sovereign at Rs. 10/4 as. But before this scheme could be carried out there followed another revolution in the relative values of gold and silver, whereby silver depreciated enormously owing to the demonetisation of silver by Germany and France. The consequent export of large quantities of silver to India led to a fall in the value of silver as compared to gold in this country. The Indian Government were very much inconvenienced by this new phenomena, since they obtained all their revenue in silver, while they had to meet heavy obligations in gold in England. Silver, which only 20 years before *i. e.* in 1852, was supposed to have a value equal to Rs. 10 per £1 if not more, fell rapidly till it touched as much as 1s. 1d. per rupee 20 years after the demonetisation of silver. To the Indian Government this was a serious embarrassment, since the fall of a single penny in the value of a rupee meant roughly a charge of a million pounds on the revenue. Naturally, they were anxious to take steps for stabilising the value of silver ; and between 1873 and 1892 they kept up a continuous correspondence

on this question with the India Office. No conclusion could be reached by this correspondence, and no agreement could be arrived at in such monetary conferences which were held at Paris, Brussels and in the United States to settle the relative values of gold and silver. At last a commission was appointed in 1892 presided over by the then Lord Chancellor, Lord Herschell; and on the report of the Commission the Indian Mints were closed in 1893, Government intending to bring about an artificial rise in the value of the rupee by restricting its coinage. For 6 years they refrained from coining and their intention, though apparently frustrated at first, was eventually realised. In 1899, in spite of the continuous fall in the value of silver bullion the exchange value of the rupee rose to 1s. 4d. or Rs. 15 to the pound sterling. This was just the value which the Government intended to give to their rupee, and so by a Proclamation of 1899 they fixed the value of the rupee at this figure, agreeing to give Rs. 15 for every sovereign tendered at the public treasuries whether in India or in England, and promising to do their best to give a sovereign in return for Rs. 15.

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## CHAPTER II.

### **General Principles of Currency.**

#### I. THE ECONOMIC IMPORTANCE OF MONEY.

We have been so familiar with the use of money from the earliest dawn of history that we are apt to underestimate the importance of the rôle which money plays in the social and economic life of civilized peoples. There are, indeed, various reasons, apart even from the familiarity which proverbially ends in contempt, which explain the common disregard of, or indifference to the importance of money. The lives and teachings of some of the greatest of mankind have consistently warned us in every age and in every clime against thinking too much of this glittering dross, for they looked upon money as the embodiment of material, perishable wealth, the source of all ill-feeling in the world, and the prompter of all the baser passions of men. Others again, like John Stuart Mill, thinking only of economics, have given us practically the same conclusion, though arguing upon totally different premises. To them money is only an instrument of exchange. In itself the money material, whether gold or silver, is, they point out, relatively valueless. It satisfies no doubt the human craving for display; but in a proper scale of human wants, graduated according to intensity, the want of adornment or ornamentation

ranks very low indeed. The pure economist therefore, agrees with the moralist in deprecating the weakness that thinks too much of an instrument, which, however useful, cannot be the end itself.

But the economist errs as much as the moralist in this deliberate disregard of a very powerful agent of social progress. The latter has no doubt some justification for his attitude, since his aim is not infrequently of this world but of the next; and he, therefore, may pardonably disregard the merely mundane things, like money. Even so, however, the judgment would be erroneous which regards money as the prompter of exclusively the baser passions of mankind. For without money the immense world-wide exchanges of to-day would be impossible. Without exchange the rapid development of industry would be inconceivable, and the onward march of civilization would be arrested. Without money charity would be difficult, self-sacrifice useless, and some of the noblest emotions absent from the human heart. Even from the moralist's own standpoint money is not a commodity utterly to be condemned. That it can be misused is not an argument to ignore altogether all its possible good uses. It is, we cannot deny, a double-edged weapon which must be handled with great skill; but in the hands of a skilful person it is bound to be productive of the best results. And the answer to the economist who wilfully disregards the importance of money is not difficult to find. Money, it is true, is only

an instrument of exchange; but it has now become so important and indispensable that exchange is unthinkable, at least to those of us who cannot think without its aid. Moreover, it is not merely an instrument; it facilitates as well as multiplies the acts of exchange. And gold and silver—the money materials par excellence—have other uses, unlike bank notes, than merely serving as a medium of exchange. To regard these metals as intrinsically valueless would, perhaps, be true strictly speaking; but because the continued custom of civilized peoples everywhere has uniformly vested them with an overwhelming importance, we would be committing a serious blunder if at this time of the day we begin to relegate money to its proper place. Unless we recast altogether human psychology; unless we all agree to classify our wants and the objects which satisfy them in the precise order in which the constitution of our organism demands them, any attempt to discount the value of money material is bound to be frustrated.

## II. THE FUNCTIONS OF MONEY.

Appreciating at its proper value the importance of money in the life of the modern industrial communities, we must yet admit that all this importance arises because money discharges some peculiar functions. Trained intelligence can no doubt grasp the idea of commerce or exchange without any intervention of a medium. We can easily conceive of

a Jack producing boots beyond what he himself would need; and wanting, therefore, to exchange the surplus for other articles of food or clothing, house-room or other comforts. It is not impossible that Jack with a superabundance of boots, and wanting to exchange boots for coats, may find James with a superabundance of coats and wanting to exchange them for boots; and also that the two may effect an exchange to their mutual satisfaction. But such a coincidence, occurring at the precise moment when it is desired, is certain to be as rare as the visitation of a comet to our solar system. And even when it occurs, the desired exchange may still not take place if the intending exchangers cannot agree upon the relative values of the commodities they wish to exchange. Having no common measure, no standard to fall back upon, they must, each time they want to make an exchange, revalue their own commodities in terms of the commodities they want to exchange them for. Such a valuation, being entirely individual and with reference to the exigency of a given moment, is sure to be disproportionate and unstable. Many commodities, moreover, are indivisible, and must, if they are to be exchanged, at all be exchanged wholly. We may no doubt divide a sack of corn, a bale of cotton, a tin of ghee into various fractions; but we cannot divide a house, or a horse, or a slave into fractions, for to do so would be to lose the value of these articles. And if to all these difficulties we add the difficulties caused by the element of time we would have a fairly accurate picture of



of exchange without a common medium. Many exchanges cannot be completed at one and the same moment of time; most exchanges in the highly developed modern commercial communities are usually, perhaps inevitably, spread over a considerable period of time. The individual, momentary valuation, indispensable in a state of barter, would be most inconvenient and utterly unacceptable in modern society.

The chief functions of money are, therefore, to remedy the difficulties of barter as sketched above. Any article which will be universally accepted as the medium of exchange may serve as money. We have records of such widely differing articles, as male or female slaves, salt-cakes, heather blocks, cowrie shells and gold and silver pieces having served at one time or another, at one place or another as money. Most of these articles have one or more obvious defects; and to the extent that they are defective their use as money would be limited. But any article may serve as a common medium of exchange, and thereby avoid the greatest inconvenience of barter, viz the absence or rarity of coincidence. We may say, then, that the first and greatest function of money is to serve as a common medium of exchange. But, as already observed, serving as a common medium of exchange is not enough. To get over the difficulties of barter we want an article which will not only be universally accepted in all exchanges: the article must also be

such as to give an exact value as far as possible, to each individual for the commodities he desires to exchange. The medium of exchange must also act as a measure of value or else the difficulties of barter will hardly be over. As such it must be capable of multiplication and subdivision. It will be impossible to decide which of these two functions is more important than the other, and so in all treatises on the subject these two are always regarded as the principal functions of money.

Two other functions, besides these, are also ascribed to money, but they are of minor importance and have as such been called the derived function of money. Money serves as a standard of deferred payments as well as a store of values. Since many exchanges in our modern societies are not completed at the same moment, but are spread over a considerable period, it is of the utmost importance that the persons entering into such exchanges should be guaranteed that the value they receive or give at one moment of time shall be, as nearly as possible, equivalent to what they give or receive at a subsequent moment when the exchange is completed. This applies not only to lenders and borrowers of money—in whose case the application is obvious—but to all commercial transactions on credit. And even in such a case as that of a farmer selling his produce for cash in the open market and wanting nothing immediately, it is but fair that at a later date when he needs any commodity the value that he has to pay must be com-

mensurate with the value that he has received for his produce. Now it is true, we have not yet succeeded in discovering the commodity which will retain its value unimpaired for all time ; but a good money material must act as a standard of deferred payment in the sense that its value in other articles must be liable to the least fluctuation. The last function of money as a store of values follows from its use as a standard ; for it embodies value in a convenient form for transport to different places or for treasuring up to be used at different times.

All these functions should be discharged by the most perfect form of money, but they need not necessarily be embodied in the same piece. We have got historical instances of countries where one commodity served as a medium of exchange another as a measure of value, a third as a standard. and a fourth as a store of value. In Akbar's time the copper dam was the common medium of exchange, the silver rupee was the standard as well as the measure of value, and the 100 tolah gold pieces like the Shahenshai Mohurs acted as a store of values. Again if our present government were to adopt the gold standard of their own without coining a corresponding new gold piece and to express the currency notes in terms of the new standard, we would probably have the notes as the most common medium of exchange, the rupee a measure of value, the imaginary gold coin a standard, and the English sovereigns or gold bars a store of value. The separation of functions does not in any way

detract from the utility of the money-material, provided the monetary organisation is on a sound basis; while a combination of functions is, in modern countries, often impracticable.

### III. MONEY AND POLITICAL AND ECONOMIC FREEDOM.

The functions of money enumerated above are too obvious to demand a lengthy explanation or to challenge any genuine criticism. There are other functions, however, which, because they are not so self-evident and universally accepted, are none the less important. The development in money-economy as against a barter-economy has everywhere served as a stimulus to political and economic freedom. It is a commonplace among the historians of the antiquities of the human race that the material progress of mankind has always taken the line of substituting contract for status, competition for custom. But this substitution would not—could not—be completed without the intervention of money. The ever-increasing number of contracts—which is a sure sign of material development—cannot be readily discharged without a medium of exchange. To give but one illustration in support of this remark all students of the history of medieval Europe, and particularly of England, are agreed that the enfranchisement of the serfs would have been of little practical value but for the rapid development, side by side, of the use of money. It



was more general spread of money that enabled the artisan and merchants in European towns to keep the feudal baron of the neighbouring castle at arm's length. It was this same agency which, by permitting the kings to enrol large number of mercenaries, enabled them to dispense with the feudal militia, and thus to effect the consolidation of the nation and the consequent birth of a national consciousness against feudal isolation, a national patriotism as against a local partisanship. And even in our own times this power of money to enable the weaker party to put up a more or less equal struggle against a stronger opponent is not without its illustration. The prevalence of the truck system in the industrial world which came into being after the Industrial Revolution gave the capitalist employer a power over his wage-earning workmen which the feudal baron never possessed over his serfs. This economic slavery could not be overthrown till the system which engendered it had disappeared and the workman was free in name as well as in fact to spend his earnings where and when and how he liked.

The foregoing remarks must not, however, be construed to show that the development of a money economy is entirely without its dark side. It has, for instance, been frequently asserted that the introduction of money has resulted in the enslavement-the more stringent because it is less obvious-of the greater portion of mankind by a very small number of their fellows. We have already said that

the truck system, a child of the Industrial Revolution, had to be killed before we could affect anything at all in the way of the regeneration of the masses. It cannot be denied that the introduction of money facilitates the storage of wealth in a convenient form, and consequently the aggregation of capital. The capitalistic regime has been frequently and passionately arraigned for having brought about vast, palpable inequalities, which, as far as we can see, are likely to be perpetuated unless drastic steps are adopted to prevent vast accumulations of capital with all its supreme command over the goods and services of the rest of mankind into a few hands. It may, of course, be urged that by itself money is the least useful commodity, serviceable only when it is exchanged for other commodities; but we must not forget that money-material is a commodity universally acceptable and always valued independent of all external circumstances. This it is which distinguishes money from other forms of wealth, in as much as while the owner of other forms of wealth must wait till there is a demand for his commodity, the owner of money need not wait at all as there is always a ready demand for his wares. And, what is more, while the owners of other forms of wealth must work themselves to produce new wealth, the owners of money, by simply loaning out their wealth, can derive a comfortable income and go on adding to their wealth without straining themselves in the least for it. Hence even if we must admit that the introduction of money has contributed largely to

the prosperity and freedom of the people in general, we must likewise admit that the same agency is responsible for emphasising, and, apparently, perpetuating the inequalities of wealth.

#### IV. QUALITIES OF THE MONEY-MATERIAL.

A discussion about the functions of money is bound to suggest the qualities required in the money-material. From the chain of arguments given above it would seem that the first requisite in a good money-material is value independent of its use as money. The value of many of our most important forms of modern money is no doubt, largely, if not exclusively, determined by custom or legislation; but custom cannot operate and laws cannot be made to establish a commodity as money without some substratum of intrinsic value. No material will be found universally acceptable unless it has some value of its own, apart from the value given to it by its constant use as a common medium of exchange. Moreover, even if almost anything would do for passage between buyers and sellers to effect an exchange not everything will do to act as a standard or a store or a measure of value. To fulfil these functions adequately the money-material must be conveniently portable, durable, divisible into pieces of various sizes and easily recognisable by its appearance. It is true that in a complex society, where the people have passed the stage when a concrete material is needed to serve

as money, and where a more perfected mechanism of exchange has restored barter for all practical purposes all these requisites may be of secondary importance; but until that stage is reached the money-material must be a concrete commodity of some intrinsic value of its own, easy to carry about, convenient to store up, undestructible, unmistakable, possible to break up into subdivisions and each division capable of retaining the indential appearance and the same value in proportion.

We need not attempt a lengthy explanation for each of these qualities. We have already given some reasons to show the necessity of some independent value in the money material, besides the conventional value which its use as money gives it. For a short period, and under exceptional emergency an apparently valueless article, like our modern paper money, may continue to circulate and discharge all functions of money; but whatever the force of convention and legal enactment may be such an article cannot be forced upon the people and circulate as money for an indefinitely long time. As regards portability it is obvious that the value of money may be influenced by its relative scarcity or superabundance in one place as compared to another. To remedy such a state of things it is necessary to counteract the superabundance in one place by means of the scarcity in another, and to carry that out it would be indispensable that the money-material be capable of easy transportation with the least inconvenience



and cost. And this is altogether independent of its use as a store of value. As regards indestructibility, if the money-material is to be constantly used in commerce, and if its value is to endure unimpaired, it is self-evident that the material chosen should be able to resist the wear and tear of daily handling. Articles of high intrinsic value, like those of food, are yet unsuitable for the purposes of money for the simple reason that they cannot last beyond a very short period of time. It is impossible to keep a large stock of such articles and it would be extremely inconvenient to carry them from place to place. The quality of homogeneity is needed because the money-material requiring to be broken up in different parts, all the sections must be of the same kind; for if not, if one piece is valued more than another, the utility of money as a medium of exchange would disappear. Divisibility also is necessary because money has to serve as a measure of value. The stability of value of the money-material is essential because if the buyers and sellers are to receive their just value for the articles they exchange the article serving as money must retain their value unimpaired at all moments of time. This question of stability has attracted the attention of writers from very early times, and we cannot yet say that we have discovered a medium of exchange absolutely proof against variations in value. Still, for a good money-material this is perhaps as important a quality as any other.

All these qualities are found, in a greater or smaller degree in what have been called the precious metals—gold and silver. They have an intrinsic worth from their lustre and brilliance and their great scarcity coupled with the cost of producing them, gives them a high value on account of which they are used for ornaments even independent of the ages old convention which has made them the material for money in all civilised countries. They are not liable to rust or decay or destruction through the ordinary wear and tear. Pieces of gold and silver are all alike, and the inscriptions and designs impressed upon such pieces make them easily recognisable. Embodying considerable value in small bulk they are convenient to carry about and thus help to keep their own value at a fairly steady level. Hence the precious metals have been generally adopted as money—material.

#### IV FORMS OF MONEY:—

##### (a) *Metallic Money.*

After examining the functions and qualities of the money material, we must next discuss briefly the various forms of money. As the precious metals fulfil almost all the requirements of a good money-material they are and have been the most important form of money. The metallic money of to-day consists chiefly of gold and silver assisted by copper, bronze or nickle for small change. Pieces of these metals, stamped with the device of a government or

any other issuing authority, and certifying thereby the weight and fineness of these pieces, are called coins. The requisites of a good coinage have been thus laid down: accuracy in composition, convenience of shape, size and weight, difficulty of counterfeiting and cognisibility. The shape and the size and the stamp and the design all combine to give the coins these several qualities. The chief evil that the coining authorities have to guard against is that of counterfeiters. The laws of almost all countries have ordained in vain heavy punishments against false coiners. This small class will continue its occupation, in spite of all its risks, so long as that occupation remains at all profitable. Mint officials must, therefore, press into their service all the devices suggested by every advance in metallurgical and chemical sciences. In order to guarantee the weight and the fineness by the impressed stamp it is essential that the right of coinage be vested in some recognised authority. The rampant individualism of the last century could not accept without question the practice of centuries past, and the question was discussed whether the right of coinage also should not be taken away from the State. Every one, however, who has studied at all the principles of monetary science; every one who appreciates the immense importance of this right in modern commercial communities; every one who understands how much depends upon the correctness of the weight and fineness the coin is certified to possess will readily admit that the right of coinage must be vested—preferably as a

monopoly—in the State. Times were, indeed, when the head of the State could wilfully debase the current coin of the realm in the hope of some small temporary advantage to himself. But the growing sense of responsibility to the public, and the increasing divergence between the functions of the State and the will of the sovereign may well assure us that a deliberate debasement of the coinage for some temporary personal advantage is now impossible. Another objection against leaving the right of coinage in the hands of the State is the possibility of immense profits arising therefrom. We may prevent such heavy profits by making the legal value of a coin conform as nearly as can be to its market value as a piece of bullion ; or by setting the profits apart as a reserve to be used for specified currency purposes. Even if we do not do so it would be better that these profits should go into the public treasury than in the pockets of private persons. Moreover it is much more economical to coin at one place than at four or five with all the corresponding multiplication of machinery &c. And finally if there is any loss through the ordinary wear and tear it would be much more just for the state to bear it than private persons. In any case the right of coining money must be a public monopoly with open mint for the coinage of standard coins. It must be a monopoly because it would be impossible to guarantee the same weight and fineness in all the coins of all the private moneyers., and the chances of debasement multiplied as often as there are moneyers.



We may mention here that though so far coins have been spoken of as if their own use was for monetary purposes, it must not be forgotten that they often serve as medals, as historical mementoes struck to commemorate a particular event. This use of a coin is becoming rarer; but the fact that the history of many of the most ancient peoples of this world has been pieced out from the slender records left by such coins proves conclusively that in the past at least this use of coins was not negligible.

#### PRINCIPLES OF COIN CIRCULATION.

The limited scope of this book would not permit us to try to unravel the mysteries of coin circulation. We must contend ourselves by mentioning only a few important laws in passing. The most important of these is the so-called Gresham's law, which may be summarised as follows: When superior money is in circulation side by side with the inferior money the latter will gradually drive the former out of circulation. It is true a slight superiority is not easily noticed by the public; but the class of money changers, bullion dealers, bankers, goldsmiths would notice the slightest difference and sort out all the best coin they get to be stored up at home or for purposes of export abroad. Their action is impossible to be counteracted by the public since, while in other things each individual can choose the best for himself, in the case of coins he is unable to

do so. Receiving them for his goods or services only to exchange them for other commodities, he is content to take any coins which are certain to pass from hand to hand. The conditions for the operation of Gresham's law must of course be fulfilled before the superior money is driven out by the inferior; one of these conditions is that both kinds of money must have full legal tender quality and the other is that the total currency must be in excess of the country's need. When these conditions are fulfilled the rest is only a question of time.

Another analagous principle of currency deals with the composition of the coinage system. Since in all countries at one time or another both gold and silver have been full legal tender currency, the question has been asked whether there is any advantage in maintaining one simple metal as the standard metal. The "Battle of the Standards" has been a long and furious one; and though monometallists seem to take it for granted that we have seen the last of it, a careful examination of the subject makes it by no means clear that we are even now completely through with the fight. To us in India the question of bimetallism *vs.* monometallism is of peculiar importance; and though discussed in other chapters we must here mention the fundamental ideas of bimetalism. The double standard has the support of historical tradition in this and other countries; but to maintain that system well in modern communities it is essential that a ratio be fixed between gold and silver at

which the two metals should exchange freely. We cannot of course fix any ratio that catches our fancy and this is one of the greatest obstacles in the way of a practical realisation of workable bimetallism. The ratio between gold and silver has oscillated backwards and forwards so violently that the bimetallists of India, the United States and the Latin Union, with the best will in the world, could not succeed in their endeavours. The ratio to be fixed must correspond to the market ratio and must be accepted by all that adopt a double standard. Unless this is done Gresham's law would operate and bimetallism will be rendered impracticable. The ratio between gold and silver in India some thousand years ago was 1: 8. Under Akbar it was 1: 9·4. and in the last century it rose to as high as 1: 30. The constant change which the last century witnessed in the relative value of the two metals rendered an agreement on a definite ratio impossible, and so the double standard was doomed. After fixing a ratio, the countries accepting a double standard must keep an open mint for the coinage of both metals, and must make the coins of either full legal tender at the ratio agreed upon. Unless the coins of both metals are legal tender at the agreed ratio to an unlimited extent the double standard will not exist in practice.

These essential conditions fulfilled, the double standard may be worked; but even then the adoption

of a double standard by any one country in the face of the single standard of all its neighbours would tend perpetually to unbalance the double standard. To be successful the double standard must prevail over a large area, and, at a pinch, the disturbed ratio in one country must be capable of correction by the import or export of the metal in question from or to the other countries.

The greatest advantage claimed for their system by the advocates of bimetallism is that a double standard prevents with ease violent fluctuations in prices. If the market value of one of the standard metals is in excess of its mint value in terms of the other standard metal, then this under-valued metal will, by the action of Gresham's law, be gradually driven out of circulation. But its displacement from currency would lead to its superabundance in the market for other purposes, and this increased supply in the market helps once more to restore the balance. This is known as the "Compensatory Action" of bimetallism, and it operates more readily in a league of bimetallist nations than in the case of a single community; for while in the former case there is nothing to be gained by seeking to export the undervalued metal from one country to another, in the latter case the requisite excess in supply may not be brought about owing to the action of exporters. And the value of the medium of exchange being thus fixed with reference to two commodities instead of one, its stability will be relatively greater. For the causes



which may affect the production or use of one of them may not affect at the same time those of the other; and, then, even if the supply and demand of one of them being affected its relative value is altered for the time, it would only be a temporary alteration, sure to be automatically rectified by the *compensatory action* of the double standard, while the general price level remains all the time entirely unaffected.

The advantage of a stability in prices is no doubt considerable enough to incline us, *a priori*, in favour of bimetallism, apart altogether from special conditions of India. But the monometallists too, must be given some credit for the special advantages of their system before we can form a balanced judgment. They point out that a single gold standard is more useful for the larger international payments which every country has to make nowadays. For gold is more easy and convenient for export than silver and consequently lends itself more readily to a readjustment in the general price level. Moreover the bimetallist system would cause frequent, though minor, fluctuations each time that one or the other metal gets over-valued or under-valued; and we cannot accept that frequent minor fluctuations are a lesser evil than the rare though considerable fluctuations of a single standard. And even as regards the compensatory action of the double standard it may be said that while it looks quite convincing on paper, in

practice we cannot depend on that action unless we can go on indefinitely substituting one metal for the other according to the changes in the market and the mint ratios. In fact it is quite conceivable that the under-valued metal, instead of being driven out of circulation may remain in circulation but at a premium. The price level under these circumstances cannot but be seriously affected; and the chief advantage of bimetallism cannot be realised. At the present moment almost all the leading countries have adopted gold standard in one form or another. Countries with an originally silver standard are no doubt even now interested in the restoring the double standard with a ratio fixed by an international agreement. But the weight and experience of the gold using countries is decisively against such a step and so we may take it that for the time being at least silver is completely ousted as a standard metal for currency.

### *(b) Paper Money.*

Another form of money consists of all sorts and varieties of paper money, whether they are convertible or inconvertible promissory notes, issued by banks or by the Government, or those numerous credit documents which, being negotiable from hand to hand, have practically all the qualities of money in the business world. There are various reasons why in civilised and progressive countries money of this kind should be substituted for metallic

money. Paper money for instance is cheaper to produce than metallic money of any kind. Apart from their rarity gold and silver are very difficult to produce and so their price must no doubt be affected by the cost of production. Paper money on the other hand is cheap in the extreme and we may take it that its cost of production is almost insignificant. The value that this form of money acquires is exclusively due to legal enactment or commercial convention. It has no intrinsic value. From one point of view, therefore, it is about the best money that could be obtained for the use of modern business world with all its intricacy. Besides a heavy cost of production metallic currency is very difficult to handle. There is always the risk of mistake in counting; there is always the chance of counterfeiting and consequent loss to honest traders by the receipt of base or false money; and, above all when money is to be carried from place to place the weight of metallic currency even in the most precious metal-gold-is a positive bar when it comes to the question of transport of large sums. In all these respects paper money is certainly superior to metallic money, provided there is full confidence in the solvency of the authority issuing such money, and provided ample precautions have been taken to guard against forgeries. If to all these qualities paper-money adds, as it no doubt does in the hands of bankers, the additional advantage of saving interest then the case for paper-money becomes very strong indeed.

## KINDS OF PAPER MONEY.

As already mentioned above paper money is of various kinds. It may be (a) representative money as exemplified by the certificates of deposits. With the exception of the United States these are insignificant at the present time in the modern highly developed nations of prime importance, though possibly they are the oldest form. (b) Promissory notes issued by banks or by the government and payable in legal tender by the issuing body on demand. Such paper is called convertible to distinguish it from inconvertible paper, which, though in the form of a promissory note, by set design or by the force of circumstances, cannot be paid in legal tender money. The question as to who should issue paper money has been widely debated in the past and not yet definitely solved. Originally paper money used to be a form of Bank money and was issued almost exclusively by banks. They would meet the needs of their customers by advancing them loans or by discounting their bills in their own paper. Since the banks can issue it only as their customers demanded, it followed that there could not be an excessive issue of such paper in a country where the banking enterprise was properly conducted. Moreover it would be an ideal form of currency since as the need of the trade demanded, it would expand and when that need had disappeared it would automatically contract, the traders no longer requiring such assistance, would return the bank paper to the bank vaults, to be



either credited to their account or in discharge of their debts. The banks would forthwith cancel the returned papers and the currency would return to its original dimensions. This is a conclusion which one might arrive at on a priori considerations, but which, however, would not necessarily be realised under all circumstances. The opponents of this principle urge it is quite conceivable—it often happens—that the bankers, being only men, even when they had the most exalted notions of their duties, could not always guard themselves against the temptation to overissue this object to increase their profit form of money, and to play with their credit beyond a degree justified by past experience in time of emergency.

Nor could we always rely upon the business world returning the bank paper to the banks so soon as the need for that paper was over. Hence would result a state of things in which banks would have issued paper beyond the need of business world, and the business community finding it a very handy convenient form of money would keep it, instead of returning to the banks, even when their needs for more money are over. The result is that there is a larger amount of currency in circulation than is wanted to effect the ordinary exchange transactions and hence there is a great danger of the price level being affected as we shall see later on.

The problem caused by these two alternative principles known as the "Banking" and "Currency" principles respectively has been solved differently

by different countries. England, for example, and Germany to some extent and the United States, accepting the currency principle have regulated their note issue in such a way that a definite minimum, known by past experience to be absolutely necessary for the needs of the country is issued against certain kinds of securities, unsupported by any form of metallic reserve. Every note issued over and above that minimum is secured by a corresponding equivalent reserve of specie. The Bank of France on the other hand is the most notable example of the successful working of the Banking principle.

#### MODES OF GUARANTEEING THE CONVERTIBILITY OF NOTES.

There are various methods of guaranteeing the convertibility of notes. Chief among these are:— (1) Limitation of the maximum amount of notes to be issued (2) Fixing the reserve either absolutely or in proportion to the amount of notes issued. (3) Providing special security apart from the reserve and (4) supporting the notes by general credit. Each of these has its own advantages and disadvantages. For instance, the plan of securing the convertibility of notes by limiting the maximum amount of notes is based on the theory that a certain amount of money being always needed by the business community, it is immaterial whether that amount is in specie or any representative money; and, therefore, since the issue of notes re-

sults in the saving of interest we might all issue the notes to that extent and economise gold thereby. In all probability, these notes will never be presented for payment; we need, therefore, it is assumed, provide neither specie for their conversion, nor any other safe-guards. There are some serious objections to these methods. In the first place the currency established in this way would not at all be elastic; and if we assume the function of currency to be the ministration to the needs of trade, such a currency can never properly minister to the needs of the business world. Again the maximum of note issue is fixed on the assumption that a minimum of money is always required by the business world. But it is just possible that this minimum may be computed so that it is really more than is needed by the community. Some notes constantly may at the same time have to be converted. As such a measure would not provide any funds or any adequate funds for the conversion of such notes this in itself would be a serious objection to such a method of safeguarding the convertibility of notes. The second method of providing a certain reserve whether a fixed minimum reserve or a proportional reserve, has this drawback, that the banks would be required, paradoxically as it may seem, to redeem their obligations on their notes until the reserve falls to a certain point and prohibiting them from doing so beyond that point. It may of course be said that the bank is bound to keep a sufficiently high reserve against all emergencies, but in practice if the banker

wants to make his business a success, he finds it difficult to maintain always a high reserve. The proportional reserve method is apt to degenerate into a fixed minimum reserve because a demand for the payment of a considerable amount of notes may so deplete the reserve as to bring it to the point of the proportion required by law, and as beyond that proportion the bankers are forbidden to utilise their reserve for the meeting of their note obligations, this method is exposed to the same objection as the fixed minimum reserve method. Other methods such as requiring a certain amount of deposits, or making the notes a general charge on the assets or making them the first charge upon the *shareholders*, have all their several points of advantages as well as disadvantages, but we cannot examine them in detail in the limited scope of this book. A combination of all these methods is frequently unavoidable and almost invariably beneficial. It is obvious that no plan can be devised which will make the notes absolutely immune from any danger, since, except by providing a cent per cent specie reserve, by their very nature the notes being based on credit, will always leave some loop-hole for danger. Every scheme of regulating paper-money has two purposes in view each of which is incompatible with the other. A note issue however secured, has to provide society with a form of currency equal to all its ordinary needs. The issuing authority on the other hand of every note issue must see to it that they provide against the dangers of inflation and depreciation of currency.



To try to reap the full benefits of one would be to run the most serious risks of the other. Under the circumstances a combination of the various methods would lead to the greatest advantage which we can expect from the use of the paper money and expose us to the least risk. Hence we should always require a certain amount of specie reserve so arranged however, that the note issue is left to expand or contract according to the needs of the business world.

## V. QUANTITY THEORY OF MONEY.

During the discussions about the forms of money we have often had to speak of the changes in the value of money. These changes are measured in terms of other commodities. But we have not so far explained how such changes are at all likely to occur. If we assume that the value of money results only from its use as a medium of exchange, and has no value apart from that function, it would be obvious that the value of money would rise or fall according as the quantity of money to be exchanged for commodities is less or more. To such a statement of this theory there are obvious objections. In the first place money, especially metallic money, has its value apart from its use as a medium of exchange. Gold and silver are required for ornamentation and other purposes; and even when they may be discarded altogether for monetary or currency purposes, they may still find some use in works of art. We cannot then say that the value of money varies

inversely with its quantity. Besides not only that the value of money, of metallic money in particular, is due to others in addition to its currency purposes but the same amount of money may by rapidity of circulation, be made to discharge far more numerous obligations. The quantity of money increases according to the rapidity with which it circulates. Perhaps the most serious objection to the theory that the value of money varies inversely with its quantity is furnished by this attribute of money which makes one and the same piece serve to discharge, five, ten, twenty or one hundred obligations. Thirdly the use of paper money and especially credit in all its forms makes us lose sight altogether of the effect of the variation in the value of money in the prices of commodities. Since credit par excellence provides a form of currency which contracts or expands precisely according to the needs of the business community, we cannot say how far the volume of money governs the level of prices wherever credit has been sufficiently developed to become a serious rival if not oust altogether the use of money. Credit must no doubt have a substratum in metallic money; but even so the transactions effected by means of credit are so enormous and the transactions effected by the use of money are comparatively so few that the quantity theory of money pure and simple cannot be depended upon. The conditions under which the quantity theory of money will hold true have thus been summarised by a leading American writer.

(1). A monopoly of the coinage or of the issue of paper-money by the central authority;  
(2). Money must serve only as a medium of exchange and have no other function or use besides those of such a medium. All the money then will be used to effect exchanges and then an expansion or contraction of its volume would have a serious effect on the price level. (3). Credit is supposed to be unknown.

As we have already seen these conditions are not fulfilled in modern commercial nations; and the quantity theory holds true if at all in a very obscure and in a very insignificant way. Still the theory embodies a very important principle of monetary science, namely that if there has been devised a form of currency which serves only and exclusively as a medium of exchange, and where credit is unknown then the level of prices would vary inversely with the volume of money in circulation. This is realised nowadays only in countries where there is an inconvertible paper currency which will satisfy nearly all the conditions required above, for it will be in all probability of government monopoly, which will have no other use except serving as a medium of exchange and which would be in use only because credit has been dislocated.

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## CHAPTER III.

### METALLIC CURRENCY IN INDIA TO-DAY.

We have already traced the history of the Indian coinage system to 1893 when the mints were closed to the free coinage of rupees on private account. To understand the present position of the metallic currency in India, it would be necessary to give a brief outline of the history of the system from 1899, when it was established, on the recommendations of the Fowler Committee, till August 1914 when the present War broke out. We shall discuss in a later chapter the state of Indian currency during this war; but for the clearer realisation of the Indian currency system this brief sketch of nearly fifteen years' working would be quite sufficient.

#### I. RECOMMENDATIONS OF THE FOWLER COMMITTEE AND THE ACTION OF THE GOVERNMENT OF INDIA.

When the Indian Mints were closed to the unrestricted coinage of silver on account of private persons, the Government of India seem to have contemplated, in the near future, the introduction of a gold standard, with possibly a new Indian gold coin,

or probably the English sovereign bodily. It was, perhaps, with that intention that the Government by a Notification of 1893 declared that gold coin and bullion would be received at the mints in exchange for rupees and notes at the rate of 1 s. 4 d. per rupee, and that the English gold coins—the sovereign and the half-sovereign—would be similarly received in payment of government dues. The falling value of silver rendered this notification inoperative for the moment. In 1892–3 the average rate of exchange for the rupee was 1 s. 3 d. In the two following years the rate fell till it averaged in 1894–5 1 s. 1 d. The rupees coined in and before 1893 continued to meet the increasing demand for the current coin. But the continued refusal by the Government to mint any more rupees all through the six years ending March 31, 1899\*, gradually raised the exchange value of the rupee, till in 1898–9 the average reached 1 s. 3.8 d., only .2 d. less than the rate contemplated by the Notification of 1893. About this time the Fowler Committee had presented a lucid, comprehensive and practically a unanimous report advocating a gold standard for India, with a concomitant gold currency. The recommendations of that commission, whose report is deservedly regarded as a classic in the

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\* No rupees were coined by the Government of India in these years except in 1897–8–9, when, under an agreement with the Native States of Bhopal and Kashmir, the currency of those States had to be replaced by the British rupee, and the Government, therefore, coined, on account of those States, some rupees in 1898.

history of the Indian currency, may be summarised as follows:—

A gold standard should be introduced in India, and the rupee should be reduced to the position of a token coin, with a conventional value of  $\frac{1}{15}$  of a pound sterling. The mints should be re-opened to the coinage of gold to the public; but they must remain closed for the coinage of silver, for the latter being only used for token currency which resulted in considerable profits to the coining authority, it was but fit and proper that such profits should be enjoyed by the State on behalf of the community at large. The profits arising from the coinage monopoly of silver were to be set aside to form a special reserve in gold-to be used if required, for the minting of a new gold coin for India, though the Committee seem to have desired and favoured the bodily introduction of the English sovereign into the Indian currency system.

Acting on these recommendations the first step of the Government of India was to make the English sovereign legal tender in India at the rate of Rs. 15 per £1. They did not, however, deprive the rupee of its unlimited legal tender quality and consequently the currency was composed for a very large portion of token silver coins with an unlimited legal tender, and a very small proportion of British gold coins, also made unlimited legal tender. It was indispensable that rupees should be coined in large quantities to meet the demands of trade and to

make up for the loss caused by the ordinary wear and tear. The coinage of rupees, however, led to very heavy profits, and so in 1900, when for the first time after 1893 the Government of India coined new rupees, the Gold Reserve Fund was instituted as a consequence in 1901 out of the profits of this coinage. This Reserve, as we shall explain more fully later on, was intended to facilitate the eventual introduction of a gold currency in India and meanwhile to keep steady the exchange value of the rupee at the point fixed in 1899. As regards the introduction of a gold currency the Government of India corresponded with the Home Authorities on the subject for the best part of 4 years; but as no agreement could be reached—whether for introducing in India the English sovereign or for minting a new gold coin for India the matter seems to have been dropped sine die early in 1903. Meanwhile, however, while the negotiations were proceeding, and perhaps by way of preparing the ground for carrying out what they thought was a certain decision, the Government of India endeavoured to introduce gold coins in India. They instructed the Post Office and authorised their Treasuries to tender gold in the first instance for every demand upon the government. It has been estimated that between January 1900 and March 1904 a sum of nearly £ 7 million in gold was put into circulation by these means in India. A portion of this sum remained in circulation; but a much greater portion seems to have been returned to



the government\*. The position of the gold coin in India is therefore as follows:—There is no special gold coin of the Government of India, but the sovereign is, by the Act of 1899, legal tender in India at the rate of Rs. 15=£1. The Government is bound to give Rs. 15 for every sovereign tendered, though since 1906 they have withdrawn the old notification of 1893 which had directed the issue of rupees or currency notes against gold whether coin or bullion. On the other hand the government is not bound to give gold coin or bullion against rupees at the fixed rate, though for administrative convenience they would do their best to issue gold at that rate in London for exporters of gold from India.

The position of the Indian currency, we must repeat at the risk of becoming wearisome, is that the bulk of the local circulation consists of the token silver coins, whose legal tender value is far above their intrinsic value. After the short-lived effort in

\* Table showing the addition of gold coins to the currency in India, ( in thousands sterling ).

Year.	Net addition to sovereigns in the hands of the public.	Year.	Net addition to sovereigns in the hands of the public.
1901-02	£ 967	1908-09	£ 3,443
1902-03	2,198	1909-10	2,866
1903-04	3,278	1910-11	8,091
1904-05	2,937	1911-12	8,881
1905-06	3,732	1912-13	11,300
1906-07	5,156	1913-14	3,907
1907-08	7,427	1914-15	5,623

1899-1904, no sovereigns have been added to the circulation, except those which have been imported in the ordinary course of trade; but even these the Secretary of State does his best to divert from India, by declaring his willingness to sell Council Bills on India at 1 s.  $4\frac{1}{8}$  d. the rupee without limit *i. e.* over and above his own needs as shown by the Home Charges. The intention of the Fowler Committee has been defeated, for in India itself there is neither a gold standard, nor a gold currency, nor a free mint for gold. An entirely new system has grown up, the operation of which, explained below, is as interesting as it is delicate.

Before, however, we describe the working of the present system it is necessary to invite attention to two points of considerable importance. The first of these relates to the reform of the coinage. No systematic attempt had been made in the sixty years that elapsed from the establishment of a uniform coinage system in 1835 to the closing of the Mints in 1893 for reconsidering the design and appearance of the coins, or withdrawal of worn out coins. Most of the older coins were greatly worn out, but as all were equally legal tender the newer and better coins went, according to Gresham's law, into the miser's hoard or the bullion-dealer's chest while the older and worn ones constituted the bulk of the currency. The Government ordered in 1896-as a first step to the reform of the coinage-that the Presidency Banks and public treasuries should not reissue any rupees of 1835 that they might re-

ceive, and five years later similar orders were issued for the first and second issues of 1840. The first issue belongs to 1835, but the issue technically called "first" issue was in 1840, and the so called second issue consists of coins minted between 1841-1861 all of which bear the date 1840. By 31st of March 1904,  $2\frac{1}{2}$  crores of 1835 rupees and 14 crores of 1840 were withdrawn from circulation. The mints, which closed to the public, were yet busy replacing the old rupees, and working also for those Native States which had agreed to demonetise their own coins and replace them by the British rupee. Between 1893-4 and 1903-4 the total out-turn of the mints amounted to Rs. 55.9 crores, of which Rs. 29.7 crores was a net new addition to the currency.

The second point relates to the currencies of the Native States. On the break-up of the Moghul Empire numerous princes assumed for themselves the right of coinage, and the right was not taken away when these principalities came under British suzerainty. Of course the local currency of those States which, like the Punjab, Nagpur or Oudh, were annexed, was gradually replaced by the British rupee. Still in 1893 there were 34 States with their own mints issuing coins bearing the device of the State and current within the limits of the State. The weight and fineness of these coins were necessarily different from those of the English rupee, and the difference caused considerable inconvenience to local trade. In 1876 an Act was passed authorising the Governor-General to declare the coins of the

Native States, of the same weight and fineness as the British rupee, to be legal tender in British India, and authorising the Native States to send their bullion for coinage at the British mints. Alwar and Bikanir were the only States that availed themselves of this privilege. When in 1893 the British mints were closed the value of the silver coins of the Native States fell considerably—below that of the token British rupee. The States and their subjects—with their obligations towards British subjects in British rupees suffered considerable loss. In the State of Cutch, for instance, the value of the local Kori—which is usually  $\frac{1}{4}$  of a rupee and the rupee—exchange value of which was fixed by the State for the purpose of paying those of its public servants who were British subjects at Ks. 379= Rs. 100 had such a decline in the value of its standard coin that in 1900 it fell to as much as Koris 600 to Rs.100. To the new conditions caused by the closure of the mints, the provisions of the Act of 1876, the Government of India declared, did not apply; but they agreed to buy their existing rupees at their current market value, and to supply British rupees instead. Sixteen States, including Kashmir, Gwalior, Baroda and Bhopal, accepted this arrangement, and only about 14 states remain outside even now.

We shall now proceed to describe the operation of the present system. The Gold-Exchange Standard, as our currency system has been academically christened, “arises out of the discovery that, as long as



gold is available for payments of international indebtedness at an approximately constant rate in terms of the national currency, it is a matter of comparative indifference whether it forms the actual national currency." (Keynes). This system, it has been said, has had to be adopted by the leading civilized countries in one form or another. In other countries, as in India, it is of the utmost importance to economise gold in order to use it for the purpose of the international indebtedness; and they achieve this either by amassing a huge store of gold, or by suspending free payments in gold in times of crisis, or by holding large reserves of foreign bills. The first of these methods is adopted almost exclusively by England, the first and second by France, and chiefly the third by Austria-Hungary and Russia. These, in times of crisis, instead of having to export gold, simply discount their foreign bills in the foreign centres and thus obtain a sufficient amount of gold to meet their obligations. This system is most convenient, it is argued, for the debtor countries, who, having always to pay more than they have to receive, must always have a ready stock of gold to meet the usual demands on them. And they might conceivably be embarrassed to meet these demands if their gold should get into the hands of the people at large and be not forthcoming at the time of the crisis. They might, indeed, accomplish their object by having a large reserve of gold to be used for such purposes; but to keep such a large amount in gold always idle in order to meet a demand which may

not be made even once in ten years, would be unjustifiable waste. Hence the growing practice for the debtor countries to keep a great proportion of their gold reserve in the shape of foreign bills, allowing very little gold to get into circulation within the country, but practically guaranteeing payments in gold for all foreign obligations. To creditor countries like England and France this is not very important, and so they still continue the more old-fashioned and wasteful methods of keeping a considerable gold reserve in specie.

The position of India is peculiar. Normally speaking she is a debtor country, who has to make immense annual payments for interest on debt, pensions and furlough allowances to her public servants, purchase of stores etc. These are collectively known as the Home Charges having to be paid in gold in England and amount to £20,000,000 in round figures. The payment for these is received and has continued to be received from the days of the Company by means of bills drawn by the Home authorities on the Government of India. These bills are known at present as the Council Bills from the Secretary of State for India in Council being the authority who manipulates these bills. From the Home Charges must be deducted the amount borrowed in England on account of the Government of India; and, as, before the war, India used to be a standing borrower in the London market every year, the total drawings of the Secretary of State for India

for the purposes of the Home Charges would be generally much less, say £ 15,000,000. But against these charges India almost always had to receive a considerable sum from England on account of her favorable balance of trade. Thus there were two streams of payments, one from India to England for Home Charges and amounting, after deductions, to £ 15,000,000 and the other from England to India the amount of which varied according to the state of the foreign trade but was usually greater than the Home Charges. The authors of the present system of currency in India saw in the co-ordination of these two streams an admirable expedient to maintain the certified value of the rupee. The Secretary of State, accordingly, announced in 1904 that he would sell bills on India *without limit* at 1s. 4½ d; and the modern exponents and champions of the Gold-Exchange Standard discovered in this the most economical and scientific system of currency, even though the system ignored altogether the recommendations of the Fowler Committee.

The mechanism of the Council Bills is thus the pivot on which the whole system turns, and we must sketch briefly the procedure for the sale of these Bills before examining critically the present system. Every week the Secretary of State announces the amount for which he is willing to sell Bills on India, with a minimum reserve price which is not published and which is seldom reached. On Wednesday morning the Bills are offered for tender at the Bank of

England. The tenders name the amount proposed to be bought and also the rate of rupee in pennies at which they propose to buy. The total amount is then allotted among the highest bidders, the Secretary of State announcing at the same time the amount he is willing to sell in the following week. This amount would be larger than that of the previous week if the demand in that week had been brisk. During the interval between successive Wednesdays the Secretary of State is willing to sell what are known as "Specials" at a rate  $1/32$  d. higher than the highest rate of allotment on the preceding Wednesday. These Bills are paid for in cash by the recipients, and are then mailed by them to be cashed in India. As in normal times the mail used to take about a fortnight in transit the Bills would not be paid in India in rupees till about fifteen days after payment for them has been made in gold in London. Those, therefore, who do not want to lose the interest on their money for a fortnight—which would at  $5\%$  be approximately £2 per £1000 or roughly  $\frac{1}{2}$  d. per £1—would be willing to pay something more for the so-called "Telegraphic Transfers" for which payment is made in India a few hours after they are paid for in England. To accomodate such people the Secretary of State is usually willing to sell the Telegraphic Transfers at a rate  $1/32$  d. per rupee higher than that of the bills. The Bills and Transfers are payable at Madras, Calcutta and Bombay at the option of the purchasers, and in rupees or currency notes.



The Council Bills have thus a much wider scope than before. Before 1900 they were only an ordinary commercial expedient to effect the transfer of money from India to England in order to pay the Home Charges. Since that date they are used to divert the flow of gold to India. The reasons for such an action are:—(1) material gain to the extent of  $1\frac{1}{2}$  per cent or nearly £ 15000 on every million sold beyond the needs of the Home Charges. For as rupees can be always had in India in exchange for sovereigns at the rate of Rs. 15 per sovereign, the banks and other financial houses will remit gold to India instead of buying the Councils if the rate asked for the latter is more than the cost of sending gold to India. That cost varies according to the state of trade, but, before the war, was seldom higher than 2 d. per £. If the Secretary of State refuses to sell under 1 s.  $4\frac{1}{8}$  d. per rupee at the time when the banks require rupees in India, gold will flow. This gold will be presented at the Indian Treasuries to be converted into rupees; and if the practice goes on for a long time, the Government of India would have to buy silver in England for coining more rupees. The payment for the purchase of the silver will have to be made by shipment of the gold which would have accumulated in the treasuries; and thus the Government of India would be losers on both sides, once by the Secretary of State refusing to sell Council Bills below 1 s.  $4\frac{1}{8}$  d. per rupee which results in a loss of say  $\frac{3}{4}$  d. per rupee, and again by the cost of transport of gold to England for the purchase of silver—another  $\frac{1}{8}$  d. or a

total loss of  $\frac{1}{4}$  d. per rupee. ( 2 ) Besides, holding gold in the currency Reserves in England has its own advantages; for, if in times of emergency like those of 1907-8, the process has to be reversed and the Government of India have to issue Sterling Drafts on London, there must be a fund to pay them from in London. In the absence of such a fund the Government of India would have to ship gold which would be costly, apart altogether from the risk of not being able to find gold when wanted for export. (3). Moreover free sale of Council Bills has the effect of transferring the balances of the Government of India from India to England which, it is claimed, results in strengthening the credit of India for carrying out any loan transactions; and even if that is not the object, such a transfer may enable the Secretary of State to earn a small amount as interest. These reasons have influenced the policy of the Secretary of State to such an extent that he has in the past sold Bills at a rate which would not only prevent gold from being shipped from England to India, but also prevent it from being stripped to India from Egypt and Australia.

In the course of the foregoing description we have referred more than once to the Gold Standard Reserve. Let us say here a word in explanation of the origin and present position of that reserve. Apart from their cash or treasury balances the Government of India have two reserves-the Paper Currency Reserve and the Gold Standard Reserve. Though

the two are now closely connected we shall treat them separately for the sake of clearness, discussing the latter in this chapter, and the leaving the former to be dealt within the chapter on the Paper Currency in India. The Gold Standard Reserve dates from 1901, when it was started under the style of Gold Reserve Fund, and was composed of the profits, arising from the coinage of rupees amounting to £3000000 which were from time to time shipped to England and there invested in sterling securities. As the demand for rupees increased, more were coined, larger profits accrued and the Gold Reserve Fund began to grow. We are not concerned here with the merits of the policy of the Government of India in respect to the coinage of rupees; suffice it to say that rupees were coined at a feverish haste and the fund began to attain dimensions at which it was thought to be safe against all attacks. On 31st March 1906 the fund amounted to about £12½ million. In the latter half of that year further heavy coinage was undertaken to meet the demands of trade. To prevent the necessity of such a heavy coinage in a short space of time a silver branch of the Gold Reserve Fund was formed, and it was proposed that this branch should have 6 crores of rupees. This limit was reached in March 1907.

The Reserve now totalled £ 17 million of which £ 12½ million was held in England in sterling securities, £ 4 million in India in rupees, and the rest in gold in India and as a book credit. For a short time

the fund was named Gold and Silver Reserve Fund, but it was finally called the Gold Standard Reserve in 1907. The events of the busy season of 1907-8 proved that the policy with regard to the Gold Standard Reserve was capable of considerable improvements. On September 1, 1907 the position of our sterling reserves was roughly as follows:—

*Gold :*

Paper Currency Reserve in India.	£. 4,100,000.
"      "      "      "      ,, London.	£. 6,200,000.

*Money at short notice :*

Gold Standard Reserve (London).	£. 50,000.
Cash Balances (London).	£. 5,150,000.

*Sterling Securities.*

In Currency Reserve.	£. 1,300,000.
In Gold Standard Reserve.	£. 14,100,000.
	<hr/>
	£. 30,900,000.

Thus the Secretary of State had nearly £ 31 million of gold before there was the faintest suspicion of a crisis occurring. Of these however only about a third was in specie the rest being either investments or short loans. Of the specie portion again there was only £ 4,100,000 in gold in India the rest being in London. Then came the crisis. The rains were scanty in the monsoon of 1907 and by the end of September all prospect of a good harvest had finally vanished. The exports from India were, falling, while the imports remain-



ing very nearly the same, the balance of trade began to suffer. Meanwhile the financial situation in America was rapidly passing through all the stages of a scare, a strain and a crisis. In the beginning of November the Bank of England, fearing an unprecedented demand for gold, raised its rate of discount to check the expected drain, and its effect was felt by the Secretary of State who on November 6 could manage to sell Council Drafts for only about £ 200,000. For several weeks after that he could not sell any bills at all, and beyond withdrawing altogether from the money-market the home authorities of the Government of India took no steps to meet the situation. Deprived of his usual source the Secretary of State was meeting his current expenses from the gold portion of the Currency Reserve in London. There was at the same time setting in a strong demand for gold in India for the purposes of export. But the situation being quite new the authorities in India were unprepared to face it. The exchange value of the rupee, which in normal times had been maintained at over 1 s. 4 d. in the London market for seven years was now steadily falling till on November 25, 1907 it reached 1 s. 3  $\frac{1}{8}$  d. The Government in India were unwilling to allow their slender stock of gold to be paid out to the clamorous exporters, though it has since been argued that the bold step of giving out gold freely in the initial stages of the crisis might have stopped it. The Government, therefore, refused to give gold for export in larger quantities than £. 10000 to any one individual in one

day. It was not till the end of December that, the crisis continuing, bolder counsel came to prevail, and Government braced themselves to take all drastic steps for maintaining the exchange value of the rupee. They declared their willingness to sell Telegraphic Transfers on London if necessary at a fixed rate, and this offer was subsequently changed into one for selling sterling bills on London at the fixed minimum rate of 1 s.  $3\frac{3}{4}$  d. per rupee. The exporters at once availed themselves of this, and within 3 months all the available reserves of gold in London were exhausted. The situation continuing weak, bills were sold in India at the rate of £ 500,000, and later £ 1,000,000 a week, and were cashed in London from the proceeds of the sterling securities from the Gold Standard Reserve. By August 1908 £ 8,000,000, out of over £ 14 million of securities, were sold to ease the situation. At the beginning of September 1908, within ten months of the crisis, the situation was, in round figures, as follows:—

<i>Gold:</i>	1907.	1908.
Currency Reserve in India	£4,100,000	£150,000.
"    "    in London	£6,200,000	£1,850,000.
<i>Money at short notice.</i>		
Gold Standard Reserve		
	(London)	£ 50,000      Nil.
Cash Balances	„	£5,150,000    £1,850,000.
<i>Sterling Securities</i>		
In Currency Reserve	... £ 1,300,000	£1,300,000.
In Gold Standard	... £14,100,000	£6,000,000.

So that against the £ 31 million odd which the Secretary of State had in September 1907, he had nearly £11,000,000 one year after. And besides the £20 million used from the various Reserves, the Secretary of State derived considerable assistance from the loans raised in England on account of the Government of India-amounting to nearly £ 4,500,000. Thus one season of depression weakened the position of the Secretary of State to the extent of £ 25,000,000, and it is beyond question that another such season in the following year would have compelled him to borrow very heavily.

We have now passed in review almost all the important points relating to the present system of Indian currency ; and though hitherto we have tried to give as colourless a description of the situation as is consistent with the character of a book like this, we would be leaving our task incomplete if we did not attempt a critical examination and estimate of all these points. The events of 1907-08 proved that the position of the Gold-Exchange Standard in India was liable to a most serious attack in the event of a world-wide crisis. But the subsequent policy of the Government, while it went on strengthening the gold resources in England, did little to mitigate what the critics of the system considered to be the standing abuses of the system. A Royal Commission was, therefore, appointed in 1913 "to inquire into the location and management of the general balances of the Government of India ; the sale in London of

Council Bills and Transfers ; the measures taken by the Indian Government and the Secretary of State for India in Council to maintain the exchange value of the rupee in pursuance of or supplementary to the recommendations of the Indian Currency Committee of 1898, more particularly with regard to the location, disposition and the employment of the Gold Standard and the Paper Currency Reserves ; and whether the existing practice in these matters is conducive to the interests of India ; also to report as to the financial organisation of the India Office ; and to make recommendations". The report of the Commission reads like an unmitigated apology of the present system, and the critics, therefore, were far from pleased. Let us, examine the grounds for criticism and the rejoinders by the advocates of the system. We may summarise the grounds of criticism as follows:—

1. The system as evolved and perfected in the years that followed the report of the Currency Committee of 1898 is in all essentials at variance with the recommendations of that committee. These recommendations—for a gold standard with a gold currency and a free gold mint—were publicly accepted by the Government, but after a short-lived, half-hearted attempt, they did nothing towards carrying out these recommendations. We propose to discuss in another chapter the proposals for a gold standard with a free gold mint and gold currency for India in which, therefore, this objection will be more fully



examined. But we must mention here that the general contention of the advocates of this system that it is the most scientific one is not well founded as far as it relates to India. In the first place, though India is a debtor country, her exports year in year out, as the following table shows, being always in excess of her imports, as far as the international balance of indebtedness is concerned, she has always to receive a balance in specie and hardly ever to pay anything, even after deducting the Home Charges.

Table showing the excess of Exports over  
Imports and Home Charges  
(in thousands sterling).

Years.	*Imports.	†Exports.	Excess.	Home charges.
1899-1900	50,200	72,463	22,263	16,129
1900-01	53,929	71,812	17,883	16,982
1901-02	59,187	83,263	24,076	16,877
1902-03	57,212	86,264	29,052	17,667
1903-04	61,728	102,344	34,616	17,399
1904-05	69,608	105,148	35,540	18,827
1905-06	74,742	107,890	33,148	17,666
1906-07	78,161	118,019	39,858	18,333
1907-08	91,025	118,323	27,298	17,768
1908-09	85,852	102,095	16,243	18,323
1909-10	81,765	125,205	43,440	18,441
1910-11	89,133	139,974	50,861	18,605
1911-12	96,037	151,993	55,956	18,865
1912-13	111,086	164,146	53,060	19,302
1913-14	127,540	166,005	38,465	19,455
1914-15	96,621	121,450	24,829	19,525
1915-16	91,700	133,000	42,300	19,403

\* The figures of Imports include Government Stores.

† " " Exports " Re-exports.

The only year in which the balance of accounts was against her was 1908-09. The necessity, therefore, which other countries have of always maintaining a good reserve in gold for meeting their international obligations—whether in specie or in foreign bills in gold—is not very intense for India. Other debtor countries must, indeed, see to it that their gold in circulation—if they have a gold currency—does not get so dispersed as to be impossible to lay hands on when required for export. But in India a demand for the export of gold—as a result of a falling off of exports—is seldom the case. And when it does occur once in a decade the resources from the Paper Currency Reserve would be more than ample to meet such a drain. We think of the resources of the Government because the Government having to meet their Home Charges are bound to be the most important factor in the exchange market. In the next chapter an attempt is made to show how, if our paper currency were based on gold were it would serve to economise gold just as the notes now economise silver. And as regards the automatic adjustment of the amount of currency to the needs of the business community, which is claimed as a special excellence of the present system, we fail to see how the agency of the unlimited Council Drafts can make our system more automatic than the ordinary agency of commercial credit. This system of the Gold-Exchange Standard, therefore, while it has no doubt great advantages for a debtor country, is not in practice so eminently suited to India as it has been claimed to be.

2. Coming to details, the location and management of the cash balances of India both in England and in this country leave much room for improvement.

**Table showing the Cash Balances of the Government of India and the budgeted surplus or deficit.**

(In thousands sterling).

Year.†	Cash Balances in India.*	Cash Balances in England.†	Surplus or deficit.
	£	£	£
1899-1900	8,426	3,331	+2,774
1900-01	10,599	4,092	+1,670
1901-02	11,880	6,693	+4,952
1902-03	12,082	5,768	+3,068
1903-04	11,870	7,285	+2,997
1904-05	10,750	10,263	+3,456
1905-06	11,781	8,437	+2,902
1906-07	10,328	5,607	+1,589
1907-08	12,852	5,738	+306
1908-09	10,236	8,454	-3,738
1909-10	12,295	15,810	+607
1910-11	13,567	18,174	+3,936
1911-12	12,280	19,464	+3,940
1912-13	19,543	11,419	+3,361
1913-14	15,608	12,477	+887
1914-15	14,715	9,163	-1,929
1915-16	12,015	12,824	-2,644

† The cash balances are at the close of the year.

\* There figures include the Reserve Treasury Balances as well as the Balances with the Presidency Banks.

† These figures include sums held in Secretary of State's balances on account of the Gold Standard Reserve.

Since 1903 it has been the policy of the Government of India to ship much of its surplus money to England and to keep it there in gold. The *raison d'être* of such a plan is, no doubt, to strengthen the position of the Secretary of State in the event of a possible drain, to enable him to earn some commission and a small rate of interest, and to allow the Government of India to avail themselves of a favourable exchange. On these grounds the Commission have reported "We find no fault, therefore, with the course taken by Government in recent years, for, under the conditions hitherto laid down for loans in India, there was no effective demand for such loans and no use for the money in that country." But in judging of these cash balances it must be remembered that they arise from surplus revenues, or an exceptional spell of prosperity in public enterprise. If they arise from a surplus of revenue, they prove that the Finance Member has been unduly cautious in his estimates; and though caution is an inestimable value in all Finance Ministers and particularly so in those of India, it is not inconceivable that caution might be carried too far. Repeated surpluses over a period of fifteen years amounting in all to £ 30·75 millions after deducting the total deficits upto 1914-15, prove that more has been taken from the people than was required. Even so the surpluses and the balances may be justified if they are used to prevent future burdens, or to lessen the present ones. The Government of India, however, have not apparently



realised that unless a surplus is used to remit a portion of taxation or to reduce or avoid the burden of debt it would be unjustifiable waste of public resources. The Commissioners seem to have taken it for granted that "as far as the ultimate object (reduction or avoidance of debt) is concerned, therefore, to which a surplus balance should be applied, we hold that it must come to London." They seem to ignore the possibility of a surplus balance being used to reduce taxation. They do not consider the question of reduction of debt in India. But even if we grant that the ultimate object *i. e.* the reduction or avoidance of debt, is best fulfilled by the surplus being shipped to London, what shall we say, of the practice of borrowing in London at the rate of  $3\frac{1}{2}$  per cent for the Government of India when the Cash Balances in the hands of the Secretary of State were allowed to remain invested at 2 per cent?

Table showing the Debt incurred in England  
( in thousands of £ ).

Years.	New Debt.	Cash Balances in England.
1899-1900	6,500	3,331
1900-01	14,422	4,092
1901-02	6,009	6,693
1902-03	5,000	5,768
1903-04	3,500	7,295
1904-05	3,000	10,263
1905-06	14,480	8,437
1906-07	2,000	5,607
1907-08	10,777	5,738
1908-09	11,342	8,454
1909-10	15,069	15,810
1910-11	13,878	18,174
1911-12	7,355	19,464
1912-13	3,000	11,419
1913-14	...	12,477
1914-15	14,715	9,163

Moreover the creation of such surpluses every year means the withdrawal from circulation a large amount of currency, and that in its turn causes a considerable stringency in the money-market in India. It is true that stringency is relieved by the encashment of the Council Drafts in India. But the demand for Councils is affected by different factors than those governing the money market. A high Bank Rate in England, or the withholding of the Indian produce in the expectation of high prices may make the demand for Councils slack, while the revenue collections would go on at their customary

pace. Moreover the demand for Councils arises only after the Indian produce is exported, while the demand for money is high in India from the time the crops have to be moved. In this respect, therefore, the policy of hoarding up considerable funds in England in the shape of Cash Balances cannot be defended. We cannot of course suggest that there should be no cash balance left in England; so long as we have to pay heavy sums by way of Home Charges we will have to remit money to England and a part of this will inevitably remain idle in the hands of the Secretary of State. We would suggest, however, that (1) the Finance Member should not—as has been the unfortunate practice in the past—budget deliberately for a surplus of over £ 500,000, if even that much; (2) that when the accumulating surplus should exceed £ 5,000,000, remission of taxation should occupy his attention in the first place; (3) that failing any satisfactory scheme for remitting taxes the sum, or at least one-half of it, should be employed to avoid fresh indebtedness, supposing further borrowing at the time was necessary; (4) that if no scheme of remitting taxes could be devised, and no further borrowing were necessary, the moneys so accumulated should be used to reduce the public debt, preference being given to the reduction of the rupee debt in order to improve the tone of the Indian money-market and to strengthen the credit of the Government of India in this country, (5) that there should not be at any time more than £ 5,000,000. as

cash balance with the Secretary of State in London, the Government of India remitting money from time to time as required for the purposes of meeting the Home Charges.

3. The next point in the working of the Indian system of currency is in relation to the sale of Council Drafts. As already explained this is the hinge on which the whole mechanism is based. They are a means of maintaining the exchange value of the rupees at or near 1s. 4½d. being sold in London at 1s. 4 d. per rupee and thus preventing the value of the rupee appreciating, and being sold in India, in an emergency, at 1 s. 3¾ d. to prevent the rupee depreciating. They have incidentally helped to convert the surplus resources of the Government of India into gold in London and at the same time prevent gold from flowing into India. The Commission of 1913, approving of these objects deprecated any predetermined limitation of the sale of Councils as "arbitrary and unnecessary", though it was recognised that "the interests of trade are in themselves no justification for sales of Council Drafts in excess of requirements as we have defined them." They, therefore, left the determination of the limits within which the Councils should be sold to the discretion of the authorities concerned. This discretion, however, is open to criticism on more than one ground.



Table showing the total sales of Councils  
and Home Charges.

Years.	Sales of Council Bills and T. Ts. 000 omitted.	Home Charges. 000 omitted.	Average rate per rupee in pennies.
	£	£	d.
1899-1900	19,069	16,129	16'067
1900-01	13,300	16,982	15'973
1901-02	18,539	16,877	15'987
1902-03	18,499	17,667	16'002
1903-04	23,859	17,399	16'049
1904-05	24,425	18,827	16'045
1905-06	31,566	17,666	16'042
1906-07	33,432	18,333	16'084
1907-08	15,307	17,768	16'029
1908-09	13,915	18,323	15'964
1909-10	27,416	18,411	16'041
1910-11	26,463	18,003	16'060
1911-12	27,058	18,333	16'083
1912-13	25,759	18,986	16'058
1913-14	31,200	19,455	16'070
1914-15	7,748	19,525	16'004

(a) The sale without limit of Council Drafts, as has been the practice since 1904, prevents the natural flow of gold in India which is detrimental to the interests of India. It is true that to allow gold to flow to India would result in the Government of India losing-on a double shipment-something like £ 15,000 on every million pounds; and as by the unlimited sale of the Councils, the Government send annually about £ 10 millions or so in excess of its requirements, it would lose, on this argument, about

£150,000 every year. But this argument is based on a misconception. The Government knows at the beginning of each financial year the amount which it has to send to England for meeting the Home Charges. To the extent of this sum the Councils must, no doubt, always be sold. In addition to these the Government of India might conceivably want gold in England for the purchase of stores and for silver bullion for coining rupees. But the former is always included in the Budget estimates of the Government of India, and is provided for in the same way as the Home Charges. The latter is, it may be admitted, an uncertain factor. But the remedy for it is a more considered and scientific policy for the coinage of rupees than the one followed so far, and not an indiscriminate accumulation of gold resources in London. We shall examine below at some length the policy of the Government of India in relation to the coinage of rupees. Suffice it here to say that if—as is quite possible,—the coining needs of the Government of India are determined in advance, provision can be easily made for the purchase of silver in the Budget. It may be urged that in view of the prevailing speculation in silver it would be impolitic to declare publicly the needs of the government in advance. But the Government would have the option of buying in any part of the year and speculators cannot keep up prices all through the year in expectation of the government purchases. Moreover Government need not coin rupees every year,

and the more prolonged the period during which purchases may be made, the less significant is the risk of loss likely to be caused by the action of speculation. But the best answer to this plea for indefinite gold resources to be held in London on behalf of the Government of India would be the discontinuance of the coining of silver altogether. We shall discuss elsewhere the methods by which this can be accomplished without dislocating entirely our currency organization; and we shall content ourselves in this place by merely remarking that, if it could be done, it would remove the most uncertain factor and so obviate the need for accumulating gold resources in London. (b). Another, and totally different objection to the unlimited sale of Councils in London is based on the fact, that in the event of a serious financial crisis in India, and with a heavy balance of trade against India, the absence or scarcity of gold in India may well render the Government of India extremely nervous about the exchange value of their local standard of currency. It is admitted on all hands that it was the relative scarcity of gold resources in India which prevented the Government in the crisis of 1907-8 allowing a free export of gold. Legally the Government is not bound in any way to give gold in exchange for rupees at the fixed rate. The issue of gold in India, therefore, in times of crisis, depends entirely on the convenience of the Government. If that convenience does not permit a free issue of gold, then for all we know, the exchange value of the rupee may fall till the

fall is arrested by the intrinsic value of the silver in the rupee. This, if it ever happens, would defeat altogether the intentions of the authors and advocates of the present system. It is to be hoped, of course, that the lessons of the crisis of 1907-8 will not be lightly forgotten, and that at the first glimpse of the likelihood of an adverse exchange to India beyond the gold export point (1s. 3½d. per rupee) the Government will offer, as they so tardily did in 1907-8 to sell freely Sterling Drafts on London at a fixed rate, not below 1s. 3⅔d. per rupee. But even so the position of the Government of India would be better, their credit materially stronger, and Indian money market appreciably easier in such a crisis if they had gold in India which they could allow for free export. The mere knowledge of an available gold fund, coupled with an official declaration permitting its free issue, would act as a charm to prevent any ordinary crisis from assuming a grave aspect. And in the case of a serious crisis the Government will have to be as good as their word, and permit a free issue of gold to genuine exporters. To do so might mean a depletion of their gold resources in one season to the extent of about 10 million pounds at the utmost, which they can easily accumulate again within a couple of years. It may, indeed, be argued that such a procedure would involve the Government of India in a needless loss of £ 80000 to £ 100000 in the year of the crisis. But such a loss, even if it does occur will occur once in 10 years at the utmost; and if at the cost of £ 8000 to £ 10000 a



year the Government could purchase a permanent improvement in their credit and ease in the Indian money-market, such a cost would, indeed, have been well-incurred. Moreover it is not quite accurate to speak of this amount as a loss to the Government; it only represents an absence of gain to this extent.

On this point, then, we may summarise our suggestions that: (1) The unlimited sale of Council Drafts in London is prejudicial to the interests of India; preventing as it does the natural flow of gold to India in the short-sighted desire to gain a small and doubtful advantage. The amount of the Home Charges, representing the gold liabilities of the Government of India being well-known, as also the amount of such other purchases as may from time to time have to be made in England, these suggest easy, practical and reliable limits to the sale of Councils in London. A slight margin of say 10 per cent of the above may be allowed for 'prudence' sake and with a view to meet unexpected difficulties. The question of purchase of the silver being an undeterminate quantity will not falsify the limits mentioned above if a well planned scheme of silver coinage is adopted; and it will be entirely besides the point if the coinage of rupees is discontinued altogether.

4. As arising out of the question of the sale of Council Drafts, which has just been considered, the question of the coinage of rupees in India may next be discussed. The coinage of rupees on a consider-

able scale after the closure of the mints to the public in 1893 was first undertaken in 1900. In the five following years there was a steady annual demand for fresh rupees, and the minting operations went on all through that period, being rather slack in 1901-2, and rather brisk in 1903-4, but never abnormal. In 1905-6 the demand gathered pace. In July 1905 the Government had silver reserve valued at £ 12,250,000 or 18·37 crores of rupees. But this heavy reserve was soon used up by the coinage operations of the months that followed. In December 1905 the whole of the bullion reserve had vanished and the rupee reserve had fallen to 7·61 crores. Meanwhile the demand for Councils in London continuing as brisk as ever fresh coinage was inevitable, and Government began to buy silver hurriedly and at a high price. But time had to be allowed for newly purchased silver to be minted and the Secretary of State had to raise the price of telegraphic transfers to 1s. 4 $\frac{5}{32}$ d. The new coinage when it became available was more than adequate to the demand and so this incipient crisis was averted. But the experience of this year led the authorities in India to believe that there was an insatiate demand for their token silver rupees, and they therefore embarked on a career of furious coinage. They forgot that while more currency is needed in times of expanding trade and general prosperity, the excess is sure to be returned to the treasuries or affect prices in times of depression. They forgot that the effects of heavy coinage in

successive years are cumulative. They overlooked the lessons of past experience, when the rupee was worth no more than the bullion it contained, when it was more profitable to melt down or hoard up and yet a succession of years requiring heavy coinage was almost always followed by reaction. In this case the reaction came soon enough. We have already sketched elsewhere the events of the year 1907-8 when the exchange value of the rupee fell below the gold export point. Rupees were withdrawn from circulation and tendered at the treasuries more rapidly than Government could give gold for them. By March 1908, Rs. 11·5 crores were withdrawn from circulation, and the figure reached Rs. 15·4 crores in the December following. Another sum of Rs. 13 crores was withdrawn, by being credited to the Gold Standard Reserve in India, by November 1908. On the whole therefore the active circulation was reduced to the extent of nearly 28·5 crores or £ 19,000,000. Since then India witnessed a continuous prosperity and expanding trade right up to the eve of the war; and as her Government, wiser by the lessons of 1908, had accepted a policy of coining rupees only when the need for them was palpable, there has been no serious danger since that time. But this story would have been recounted in vain if it does not disclose that the policy of coining rupees has in the past been open to just criticism. The following table shows the amount of rupees coined every year; and the figures might, by careful handling, be made to supply a good working rule for new coinage every year.

Whole Rupees coined and issued from the  
Indian Mints from 1835.

000 omitted.			000 omitted.		
1835	...	16,39,78	1892	...	10,46,55
1840	...	31,16,70	1893	...(a)	7,87,30
1840	...	76,65,60	1897	...(b)	15,24
1862	...	70,69,12	1898	...(b)	75,19
1874	...	4,35,22	1900	...(d)	11,81,39
1875	...	3,09,91	1901	...(e)	10,91,35
1876	...	4,09,50	1902	...(f)	9,31,39
1877	...	13,48,06	1903	...	25
1878	...	9,65,85	1903	...(g)	10,23,47
1879	...	8,87,28	1904	...(h)	16,02,78
1880	...	7,21,85	1905	...(i)	12,74,60
1881	...	5,597	1906	...(j)	26,37,50
1882	...	7,14,87	1907	...(k)	25,22,49
1883	...	2,31,46	1908	...	3,09,32
1884	...	4,84,88	1909	...(l)	2,22,97
1885	...	9,90,30	1910	...	1,76,88
1886	...	5,20,24	1910	...	58,23
1887	...	8,86,00	1911	...	94,43
1888	...	7,07,68	1912	...(m)	12,41,89
1889	...	7,46,68	1913	...(n)	16,32,65
1890	...	11,76,41	1914	...	4,83,70
1891	...	6,41,69	1915	...	1,52,72

(a) Includes Rs. 590 thousands for the Bikaner State.

(b) On Account of Kashmir and Bhopal recoinage.

(d) Includes Rs. 2,09,02 thousands coined for Native States.

(e) " " 1,90,43

(f) " " 2,98,86

(g) " " 11,66

(h) " " 5,94

(i) " " 3,28

(j) " " 3,90 thousands coined for Native States  
(Calcutta 32 Lakhs and Bombay  
135 Lakhs) Coined from Gold  
Standard, Reserve Silver.

(k) " " 94 thousands coined for Native States  
and 433 Lakhs coined from Gold  
Standard Reserve Silver.

(l) " " 1,01 thousands coined for Native States.

(m) " " 16,56

(n) " " 12,73

" " "

" " "



Without any reasonable, well founded estimate of the capacity of the country to absorb new rupees, without even any reference to their own experience in the busiest season of 1905-6 Government coined rupees and thus deliberately depleted their sterling reserves; for every rupee added to the circulation meant corresponding withdrawal from the gold reserves. Not to coin fresh rupees when trade is expanding may possibly expose the traders and merchants to some temporary inconvenience. And if this inconvenience amounted to serious emergency Government could always buy silver when wanted and resume their coinage operations, the Indian mints being able to turn out 13 lakhs a day without overtime. It is true that to go into the market to buy silver at a moment's notice may oblige the Government to pay a fairly stiff price. But even that loss is preferable to the risk of indiscriminate coinage of rupees which would be the alternative. Besides the necessity to buy silver at a moment's notice is not inevitable, for by the exercise of a little foresight, the needs for rupees may be estimated in advance for all practical purposes. And if such an estimate is impossible we have to choose between two evils—the possible inconvenience to traders for want of rupees and the probable depletion of the sterling reserves. The two evils need but be mentioned thus side by side to show which must be selected if a choice is inevitable. We may then summarise our conclusions in this section as follows;—

(a) The Government of India would do well to adopt the policy of the French Government in minting their silver coins. This suggestion, however, cannot be explained without a discussion of the need for a gold standard and a gold currency in India. We shall accordingly postpone it to the chapter dealing with that subject. (b) If the coinage of rupees is inevitable it should be carried out in accordance with a well-considered preconcerted plan, based on the experience of the absorption of rupees in the past.

#### IV.—GOLD STANDARD RESERVE.

The next point on which the present system has been adversely criticised is in connection with the Gold Standard Reserve. Discussion on this subject divides itself into three convenient sections such as (a) the nature and object of the Reserve; (b) its composition and its amount; (c) its location.

(a) As regards the nature and object of the reserve the Fowler Committee intended it to be built up out of the profits of the silver coinage, to be kept in gold; and, when it had reached a certain respectable amount, it was to be used for the introduction of a gold Currency in India. Says that Committee in para (59) of its report, "Although the Government of India should not, in our opinion, be bound by law to part with its gold in exchange for rupees, or for merely internal purposes, *we regard it as the principal use of a gold reserve* that it should be freely available for foreign remittances whenever the exchange falls below specie point, and the Government of India should

make its gold available for this purpose when necessary, under such conditions as the circumstances of the time may render desirable.....and, when it has accumulated a sufficient gold reserve, and so long as gold is available in its treasury, it might discharge its obligations in India in gold, instead of in rupees". This recommendation, read in conjunction with their suggestions about making sovereigns legal tender in India and allowing them to be coined at the Indian mints, makes it impossible to construe the last clause as a revocable permission to use gold in India. Even though the Committee of 1898 declared that rupees must remain unlimited legal tender for some years to come, mere tokens as they were, we cannot take the meaning of the Fowler Committee, reading their recommendations as a whole, to have designed the Gold Reserve Fund exclusively for supporting the exchange value of the rupee in gold. The policy, however, of the Government of India, in the years that followed, made it increasingly clear every year that there was no intention to use the Gold Standard Reserve, as it later on came to be called, for introducing gradually a gold currency in India. And the Chamberlain Commission of 1913 gave the seal of its approval by remarking. "The experience of 1907-8 makes it clear that the Reserve is required not merely to meet the "Home Charges" of the Government of India, at a time when an adverse rate of exchange prevents the free sale of Council Drafts, but also to liquidate an unfavourable balance of trade to the extent neces-

sary to prevent exchange from falling below specie point. On the other hand the Reserve is not required to provide for the conversion into sovereigns of rupees in circulation in India. Gold is world's money, and *India like other great countries, needs gold less for internal circulation than for the settlement of external obligations* when the balance of trade is in sufficient to meet them." But here we are confronted with a radical difference of principle. Those who regard the Gold Standard Reserve as having been designed to facilitate the eventual introduction of a gold standard can never appreciate the views of those who destine it exclusively for steadying exchange. The latter assume that gold is not needed for internal currency purposes by any country, while the former see in the current circulation of gold in a country the only guarantee of a steady exchange without any need of helps from the manipulations of public authorities. This is a point, which, perhaps, had best be discussed under the chapter dealing with the need for a gold currency in India.

Coming next to the amount and composition of the Reserve, it is needless to postulate that the amount and composition of the fund must necessarily depend in a great measure upon the object it is meant for. But assuming that object to be what the official spokesmen have formulated it to be, viz. the steadying of the exchange value of the rupee, the manipulation of the Reserve is open to criticism. As already mentioned the Reserve dates from 1900 and the following Table shows its growth and position in the succeeding years.



Table showing the amount, composition and location of the Gold Standard Reserve.

Date.	In England ( in thousands sterling ).				In India ( in thousands sterling )				( In thou- sands sterling ).
	Securities at Market Price.	Cash at short notice.	Gold at Bank.	Total.	Loans and Book Credits	Gold.	Silver.	Total.	
31st March.	£	£	£	£	£	£	£	£	Grand Total.
1901	...	...	...	...	1,830	1,200	...	3,030	3,030
1902	3,456	...	...	3,456	...	...	...	...	3,456
1903	3,652	...	...	3,652	1	...	...	1	3,653
1904	6,041	...	...	6,041	167	...	...	167	6,209
1905	8,387	...	...	8,387	152	...	...	152	8,539
1906	12,122	...	...	12,122	286	...	...	286	12,409
1907	11,960	...	...	11,960	301	21	4,000	4,323	16,283
1908	12,978	1,131	...	14,110	...	...	4,000	4,000	18,110
1909	7,133	469	...	7,603	...	...	10,586	10,586	18,190
1910	12,695	3,010	...	15,706	...	...	2,534	2,534	18,240
1911	15,407	1,477	...	16,885	...	...	1,934	1,934	18,819
1912	16,087	1,073	...	17,161	...	...	1,934	1,934	19,095
1913	150,945	1,005	1,620	18,571	...	...	4,000	4,000	22,715
1914*	13,370	907	2,300	16,577	3,025	6,233	...	9,258	25,836
1915	12,148	8	1,250	13,406	7,069	5,238	...	12,307	25,613
1916	16,218	5,792	...	23,010	4,001	238	...	4,239	27,249

\* Figures for October 31st.

And by the time of the crisis in 1907-8 it had reached nearly £ 18 millions. It was decided about this time that a part of the profits on coinage should be used for railway construction in India, but this step proving perilous, the idea was soon afterward abandoned. The Gold Standard Reserve however went on accumulating till on the 31st March 1914—some four months before the war, the Reserve stood as follows:—

Sterling securities at market-value	£ 17,745,543
Money at short notice and gold	
with the Bank of England	... £ 4,344,962
Silver in the Indian branch	... £ 4,000,000
	<hr/>
	£ 26,090,505

Out of a total of over about £ 26 million more than  $\frac{2}{3}$  was invested. In the event of a serious crisis the invested portion would not be available without a serious loss. Even therefore if we take it to be meant for steadying the exchange value of silver, this disposition of it is open to serious reflection. The idea of investing a portion of the Reserve no doubt originated in the desire to earn interest. But the loss on a forced sale during a crisis, not to speak of the great depreciation which all securities—even the best—are liable is often more than the whole of the interest earned during the period the money was lying idle. To take but one example, in the crisis of 1907-8 securities to the nominal value of £ 8,000,000

were sold. During the five years preceding that amount would have earned interest at 3 per cent amounting to £ 240,000 per year or £ 1,200,000 in 5 year. According to Alakh Dhari the forced sales of securities in 1907-8 resulted in a loss of Rs. 22 lakhs or over £ 150,000. Says the Decennial Report of the moral and material Progress of India for the years 1902-3 to 1911-12. "Upto 31st March 1912 there was a net profit of £ 2,105,868 on the investments; £ 2,958,138 had been received as interest and discount, while the securities held had depreciated to the extent of £ 680,702, and losses amounting to £ 150,083 had been incurred on the sale and redemption of securities. Miscellaneous charges had amounted to £ 18,480." On the 31st March 1916, the securities of the value of £ 17,007,837 had depreciated by nearly three quarters of a million, being estimated on that date at market price at £ 16,218,692. And the depreciation has been much greater since. The shock to public confidence by such depreciations remains as great as ever. The investment of this Reserve in even the best securities is reprehensible, and the Chamberlain Commission reported "We are of opinion that the actual gold held in the Gold Standard Reserve should stand at a much higher figure than £ 5,000,000.....In our opinion the best rule in the present circumstances would be that no less than one-half of the fund should be held in actual gold when the total fund exceeds £ 30,000,000, and that a minimum amount of £ 15,000,000, should be accumulated as rapidly as

possible". This leads us to the discussion of the amount of the Reserve. There are three tests by which we might determine the amount viz. (1) the conversion requirements of the token currency (2) the trade needs of India, (3) the Home Charges. All these tests, of course, are not mutually exclusive. To begin with the first it has been asserted that the total amount required in the Gold Standard Reserve would be some £ 120,000,000 to £ 150,000,000, if all the rupees and notes in circulation were made convertible on demand into gold. This estimate, however, is based on the misconception that if conversion is permitted all the rupees and notes will be immediately presented for being exchanged into gold. Some paper money must remain in circulation, for even gold is too cumbrous for large payments. On the other hand a great portion of the rupees also must remain in circulation, for the ordinary transactions in India are of such small sums that no gold coin could serve the purpose. If, therefore, free conversion in gold is permitted not more than a third of the total money in circulation could ever be presented for conversion. We need not, therefore, have a bigger reserve in gold than £40 to 50 millions. On the other hand if we take the trade balance of India as a test, India has been for all the ages past and is likely to continue to be for some generations to come a country with a favourable trade balance. No reserve in gold need at all be accumulated on the score of trade alone. If there were no Home Charges to pay, India's trade even in the worst years of famines, would finance itself. There



may indeed be a temporarily adverse exchange ; but it would soon be redressed by the returning wave of prosperity. It is really the Home Charges which makes our exchange problem a source of great anxiety. Even on this basis of the Home Charges, however, the utmost that can be required from India in that way amounts to £ 20,000,000 a year in round figures. If we assume that there will be no balance of trade in favour of India for two consecutive years—a most improbable assumption—we would need £ 40 millions to pay our Home Charges, supposing that during that period we did not borrow at all in England. The safe figure to which the Reserve should be accumulated is on two independent tests, found to be somewhere between £ 40,000,000 and £ 50,000,000. It should, of course, be held exclusively—or at least predominantly in gold. The loss of interest on £ 50 million at 4 per cent would be £ 2 million a year: but in the interests of the stability of exchange such an outlay may well be made without hesitation ; while the loss may be reduced by providing that a third or at most a half should be invested in Indian and English securities.

The last point of criticism on this question of the Gold Standard Reserve is in connection with the location of the fund. It has been the practice ever since the creation of that fund to keep it in England. The Chamberlain Commission has approved of this practice by declaring, “ The most suitable place for the location of the Gold Standard Reserve is, in our opinion, undoubtedly London”, and they

support this contention by urging "London is the clearing House of the world, India's chief customer is the United Kingdom, and London is the place where money is required both for the expenditure of the Secretary of State on India's behalf, and for payment of India's commercial obligations to this country and the world in general. If the Reserve is kept in India it would have to be shipped to London to be used. This would involve delay at a moment when immediate action is necessary.....

..... We have no hesitation therefore in recommending that the whole of the Gold Standard Reserve should be kept in London". This recommendation, however, is founded on a misconception. (1) The presence of the Reserve in India would be a source of immense moral strength to the business community in India. (2) And the shipment of gold to London will not be required, if past experience through an unbroken series of generations is at all reliable, more than once in ten years. (3) Besides if the Reserve is in India it might enable our Government to meet its obligations in gold, and thereby reduce the rate of interest. (4) Lastly the Reserve in India, if any portion of it is to be invested, will be invested in rupee securities, and so strengthen the credit of the Government in India. In view of all these arguments the policy of keeping the whole of the Reserve in London cannot but be unhesitatingly condemned.

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## CHAPTER IV.

### **Paper Currency.**

#### I HISTORY.

The history of our Paper Currency proper dates from 1839-1843 when the three Presidency Banks were allowed to issue notes payable on demand. These notes, not being legal tender, could be used only in those centres of commerce where, as in the Presidency Towns, some substitute for metallic currency was required to facilitate large payments. After the Mutiny, the disordered state of the finances of the Government of India claimed and obtained the assistance of a special Finance Minister. Among the many constructive measures of our first Finance Minister-Mr. James Wilson-was an attempt to regulate and popularise the excellent substitute for metallic money which was provided by the paper notes of the Presidency Banks. Their notes, he learnt, had not made any encouraging progress, but he rightly judged that this slow progress was due to the absence of the legal tender quality. To make the notes legal tender would raise the new and hard problem of their convertibility, and the consequent necessity of public confidence in the issuing authority, its solvency, the provision of an ultimate reserve etc. The notes issued by these Banks were not supported by any strong reserve as they were



required to keep a combined reserve of only 25% against all their outstanding demand liabilities. Considering the situation of India after the mutiny, Wilson judged it best that the note issue should be centralised and made a public monopoly, not only because of the immediate gain to the state represented by the saving of interest on that portion of the reserve which was invested, but also because of the immense need of insuring confidence and thereby the popularity of the notes. No private institution, not even the most respectable Bank, could inspire that confidence which was essential for the popularity of this new form of money; and it was but fair that the profits of the note-issue should be taken by the State, since they would be a kind of tax levied on the general public.

Mr. Wilson and his colleagues in the Viceregal Council in India as well as Sir Charles Wood, the Secretary of State, were in complete agreement about the necessity of making the Indian note-issue a public monopoly. But they could not bring themselves to view from the same stand-point the question of reserve. The authorities in England, with their memories of the Paper Currency controversy in England after the publication of the Bullion Commission's Report, could not conceive of any measure as sound which did not accept the principle of the Bank Act of 1844. They wanted the notes to be covered, pound for pound, by an equivalent metallic reserve, beyond a very small fraction which might

be issued against securities. Even this small portion was suffered to be issued against securities and without a metallic reserve, when it was proved that this portion represented a minimum which under no conceivable circumstances was likely to be presented for conversion. In vain was it pointed out to them that such a measure made the currency inelastic in the extreme, incapable of expanding with the needs of the community unless there was a specie to back it; in vain did Wilson plead that the very object of a representative money—the economy of the precious metals—would be defeated by such a measure, and that the profits to the issuing authority would be unnecessarily circumscribed. Sir Charles Wood remained adamant on this point of the metallic reserve, and Wilson was spared the mortification of carrying out a scheme of which he could not approve by the timely breakdown of his health.

On all other points there was a substantial agreement between the authorities in India and in England; and the Paper Currency Act was passed in 1861, repealing all the previous legislation on the subject, and inaugurating an entirely new system. The salient points of this system were: (1) The Currency notes were made legal tender to an unlimited amount in their respective circles of issue and were issued by the Government exclusively. (2) They were in the form of a promise to pay on demand at the head-quarters of the circle from which they were issued. Notes of one circle were not legal tender in

another circle, except for the payment of Government dues which could be paid in any circle in the notes of its own or any other circle. Railway Companies, too, might receive in payment of their fares and traffic charges, notes of any one circle in any other, and recover specie from the Government against these notes. The public treasuries, also, would in practice cash the notes of *any other circle* as well as their own, provided they had funds to do so. There were four such circles, viz., Calcutta, Bombay, Madras and Rangoon; and four subcircles, viz., Cawnpore, Lahore, Karachi and Calicut. By an Act of 1910, which consolidated the law on the subject of the Paper Currency, the sub-circles were abolished; and so now there are seven circles in all, viz., Bombay, Calcutta, Cawnpore, Karachi, Lahore, Madras and Rangoon. This arrangement of dividing the country up into several provinces is open to the objection that the area under which the notes are unlimited legal tender being restricted, the notes can never become very popular, nor can the economy of metallic money be very considerable. On the other hand the experiment of a public note-issue in India was new. The credit of the Government, after such a shock as that caused by the Mutiny, could not be wilfully exposed to the least possible and preventible danger. The demand for cash (rupees) varied in different parts of India at different seasons of the year. Would it then be prudent to create a system, which, by giving full facilities for cashing the notes, may make them so popular that their very popularity may be a



menace to the credit of the State? Of course when once the notes were rooted deep in the confidence of the public, when they had learnt to use notes for other purposes than immediate encashment, it would be time enough to recast the system. As we shall see below this was what actually happened nearly half-a-century after the first Paper Currency Act was passed; and that during this long interval the notes did not make any rapid progress in popularity does not constitute an unlimited censure on the authors of the system in 1861. (3) The notes were originally issued in the denomination of Rs. 10, 20, 50, 100, 500 and 1000. The small denomination of notes-being as low as s. 20/- according to then valuation of rupee in terms of the pound sterling, was necessary in view of the poverty of the people of India and the smallness of their daily transactions. The five rupee note was introduced in 1871 and later on the ten thousand rupee note. The five rupee note was made universal legal tender, except in Burma, in 1903. By the consolidating Act of 1910, the issue of twenty-rupee notes was discontinued, and the ten and fifty rupee notes were made universal legal tender-that is payable in any circle whether of their origin or not, and power was given to the Governor-General-in-Council to declare notes of higher denomination universal legal tender by an executive order. In pursuance of this power notes of one hundred rupees were made universal legal tender in 1911. The Act of 1910 also removed the Burman limitation on the five



rupee notes. In 1911 the Government forbade the receipt of notes of higher denominations, in circles other than the circle of issue, in payment of government dues or to Railways or post and Telegraph Offices. (4). The whole amount of the Currency notes in circulation is secured by a bullion reserve and securities of the Government of India and of the United Kingdom. Originally the Paper Currency Reserve consisted almost exclusively of silver, but the policy was inaugurated in 1893 of issuing notes against the British sovereigns and gold at the rate of Rs. 15 per £, so that now it consists of gold as well as silver. In 1861 the total amount of the Reserve in securities was fixed at Rs. 4 crores—that being deemed the indispensable minimum of notes which in all probability would never be presented for conversion in metallic money. The growth of the note—circulation twenty years later was sufficiently gratifying to permit an increase of the invested portion of the Reserve to Rs. 6 crores. The issues, however, went on still expanding, and power was, therefore, given to the Government of India, by Act IV of 1890, to raise the limit to Rs. 8 crores. This power was first utilised in december 1890 when it was raised to Rs. 7 crores, and again a year later to Rs. 8 crores. Act XXI of 1896 empowered the Government to raise again the Reserve to 10 crores, and the power was exercised in December of that year. In 1905 by Act III of that year another 2 crores was added to the invested portion, this sum being invested by the Secretary of State in Consols

and Exchequer Bonds. In 1908-9 the Exchequer Bonds were replaced by Consols. By Act VII of 1911 the limit was further raised by two crores and the Secretary of State was allowed to invest another 2 crores in Consols. Thus the total invested Reserve of the Indian Paper Currency stood at Rs. 14 crores just before the outbreak of the war, and of these only 4 crores were invested in sterling securities. As regards the metallic Reserve, under the Gold Note Acts of 1898 and 1900, power was given to the Government of India to hold a part of the metallic Reserve in gold coin, or temporarily in silver bullion in London instead of in India. The object of these Acts was to afford some relief to the Indian money market in seasons of stress, if notes could be issued against gold tendered in England, the Secretary of State could sell the Councils freely in London. Some gold was held in London under these acts, but not as a part of a permanent policy. An Act of 1905 however formulated a permanent policy on the subject, by fully empowering the Government to hold the metallic portion of the Reserve, or any part of it, at its free discretion, either in London or in India, or partly in both places, and also in gold coin or bullion, in rupees or silver bullion, provided that all coined rupees should be kept in India alone. Under the provisions of this act a Paper Currency chest was instituted in London, and a sum of £6,000,000 in gold was remitted from India to be held in that chest. A further sum of £1,045,000 was transferred to the chest from the

Secretary of State's balances in 1905-6. This gold began to increase in amount after 1906 and on 31st March 1913 a year before the outbreak of the war, the total Reserve was distributed as follows:—

	In crores.
Silver in India	Rs. 16.45
Gold     "     "	Rs. 29.37
"     " London	Rs. 9.15
Securities	Rs. 14.00
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Total Rs.	68.97

## II. ORGANISATION OF PAPER CURRENCY OFFICE.

Before we go on to discuss the problem of Paper Currency in India, it would be interesting, though a point merely of detail, to note that the issue of the Currency Notes is managed by a Paper Currency Department, whose function it is to issue notes without limit from any Paper Currency Office against rupees, half-rupees and sovereigns. Notes may be issued even against gold-bullion and gold coin, which is not legal tender from circle offices on the requisition of the Comptroller-General, who is the head of the Paper Currency Department. The notes are supplied by the Secretary of State through the Bank of England on an indent by the Head Commissioner. He in his turn or the Commissioners under him supply notes as required to all the Currency Agents in the country. Every note, except a universal one, bears upon it the name of the place from which it is issued, while every note without exception has impressed upon it the

signature of the Head Commissioner or of a Commissioner or Deputy Commissioner.

### III. PROBLEMS OF PAPER CURRENCY.

#### (a) *Popularisation of Notes.*

It is now fifty-six year since the Paper Currency Act was passed, and almost eighty years since this form of currency was first introduced in India. Yet during that long period the development of currency notes has been not all that could be desired. At its inception in 1862 the total gross circulation of notes was Rs. 369 lakhs. After 30 years it was 2710 lakhs, and thereafter the growth has been as follows:—

#### AVERAGE CIRCULATION IN CRORES OF RUPEES.

YEAR.	GROSS.	NET.	ACTIVE.
1892-93	27.10	23.33	19.53
1893—4	28.29	20.83	17.85
1899-1900	27.96	23.67	21.27
1900-01	28.88	24.73	22.05
1902-03	33.74	27.35	23.49
1904-05	39.20	32.76	28.11
1906-07	45.14	39.49	33.93
1908-09	44.52	39.02	33.10
1909-10	49.66	45.35	37.21
1910-11	54.35	46.48	38.75
1911-12	57.37	49.49	41.89
1912-13	65.62	54.92	45.39
1913-14	65.55	55.62	46.63
1914-15	64.04	59.28	45.43
1915-16	64.10	60.39	48.08



On 31st March 1914 the gross\* circulation *i. e.* the total number of notes issued was valued at 66 crores. The need for developing the note-issue is felt in India because her currency system is so very inelastic. According to the provisions of the law no new notes can be issued unless an equivalent quantity of specie is presented in exchange. Though the amount of investments held in the Paper Currency Reserve was considerably raised during the war, as we shall describe more fully later on, and though the gross circulation on the 25th January 1917 was Rs. 83,40,17,570, the paper portion of the total currency is only about  $\frac{2}{5}$  of the whole. Besides Indian business public is not yet so widely accustomed to the cheque system, which has completely counteracted the similar inelasticity of the English currency system; nor can we believe that the Indian public can or will adopt the cheque as a means of payment on a much wider scale in the near future. Meanwhile the trade of India is expanding every year. The foreign sea-borne trade alone has increased from Rs. 122·59 crores in 1875-76 to Rs. 480·83 crores in 1913-14 the year before the war. And if to this we add the far more numerous transactions of exchange within the country, it is obvious that the commercial world, with its ever increasing transactions, would

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\* The net circulation, it may be remarked, is the total number of notes in circulation less those held in Government Treasuries, while active circulation is the net circulation less the notes held by the Presidency Banks.

be sorely hampered by the lack of a medium of exchange which could be easily contracted or expanded as occasion required. Various suggestions have been made for affecting this most urgent reform. The Chamberlain Commission recommends, "We think it eminently desirable that the use of notes in India should be encouraged by all legitimate means. With this object in view, we recommend that the Government should increase, whenever and wherever possible, the number of places at which the notes are encashable of right as well as the extra-legal facilities for encashment. We think it would be desirable to universalise at once the notes of 500 rupees. With the experience gained it may be found possible to carry universalisation still higher". Against this proposal the only objection that could be taken is that the Government might have to keep a large reserve available at any moment in any treasury, and that they might have to incur a heavy cost of remitting specie from district to another frequently. With a little more experience, however, the authorities could easily make adequate provision, without keeping an unduly large reserve, against all possible emergencies of this nature. The great facilities offered to the business community by such a reform, and the consequent increase in the quantity of notes in circulation, would more than counterbalance the cost of remission that may have to be incurred from time to time.

Not the same thing, however, can be said for another proposal that has attracted some public

attention of late, and which has been, apparently, approved of by the Finance Minister. On the assumption that India is a very poor country where the ordinary transactions are of extremely small amount, it is contended that the present notes of even the lowest denominations are of too inconveniently large amounts to be universally acceptable in India. And this contention is attempted to be driven home from the analogy of France, where even in times of peace the lowest denomination of notes was 5 francs equivalent to Rs. 3, where the people are much richer and consequently their average transactions are of much larger amounts than those of the Indian peasant, and where during this war the issue of notes of even so low a denomination as 1 franc, or ten annas was sanctioned. Such an extension of the note-issue would be necessary if the object of a note-issue is the economy of metallic currency, especially during the extraordinary circumstances caused by a war. Japan, it is said, had issued notes of as low a denomination as 10 sen during the Russo-Japanese war. Moreover towards the end of last year the growing export trade of India had assumed such dimensions that the stock of rupees in India was rapidly exhausted by the unrestricted sale of Council Bills, until in December 1916 at last the Secretary of State had to restrict his sales. This, however, intensified the crisis. The tightness in the money-market in India became tighter than ever; banks began to call in their short loans, or to demand an increase of margin for advances against

industrial securities; the value of these securities began to tumble and the general situation of the export trade of the country was imperilled. It was under these circumstances that the proposals for one rupee and two rupee notes were mooted; and, the situation continuing unchanged all through January and February, the Finance Minister accepted the idea in his Financial statement in March 1917.

We have mentioned at length the circumstances in which the suggestion originated, and also the assumptions on which it is based, in order to render our criticism more intelligible. It must, of course, be admitted that the present state of India's trade and currency are such that without some increase in the medium of exchange there is every risk that the present wave of prosperity may be wilfully turned away from us. There is also some truth in the statement that the bulk of the transactions of business life in India are of such small amounts that a one rupee note may be more convenient than five rupee notes. But when we have admitted all this we have done all that could be done for such a proposal. For it is a short sighted proposal based only on the perception of the immediate necessity and prompted in a great measure by a slavish desire for blind imitation of the example of other countries in this respect.

(1) In the first place to carry out such a proposal we must have a radical reform in the very basis of our whole paper currency system. The issue of one rupee notes—or even of one anna notes—would in no



way help the situation, so long as the law requires that every note issued, beyond a certain fixed minimum, should be covered by an equivalent amount in specie. Government cannot issue such notes unless they either increase the invested portion of the Reserve, or else alter the law so as to allow a certain proportion of the total reserve—and not a fixed amount—to be invested. Such a change, we have no hesitation in declaring, it would be most unwise to carry out at this time of stress and strain, when proposals of such far reaching importance, which require long and careful deliberation, are apt to be hustled through the Legislature with little or no criticism. (2) But even supposing the proposal is adopted, the expected relief may not result all at once. Precisely because notes of such small denomination would be an entirely new experiment, there could be little chance of their being so widely accepted as to bring an immediate, perceptible relief to the currency situation. And even if the Government forces such notes into circulation by every device in their power, they would be soon returned to the treasuries or cashed at the Currency Offices. If the Government keeps an adequate, equivalent Reserve for their encashment on demand there would be no solution for the currency problem at all. If on the other hand, the Government increases the invested portion of the Reserve, it would risk its credit unnecessarily. Out of a total circulation of Rs. 83,40,17,570 on January 25, 1917, Rs. 42,32,57,421, were invested, or more than half of the total. Should this amount be raised for

the sake of a new issue of one and two-rupee notes, say to the extent of Rs. 7 or 8 crores, the metallic portion of the Reserve is almost certain to be drained to that extent, and its proportion to the total circulation would be reduced to  $\frac{1}{3}$  or a little more. And if the one and two-rupee notes are forced into circulation still more we may be within sight of an inconvertible paper currency which needs but be mentioned to be disapproved of. (3) The example of France during this war, or Japan during the Russo-Japanese War are misleading. With an educated people and a national Government, which is sure to be supported whole-heartedly by the entire people in an emergency like that caused by a great war, those Governments could fearlessly attempt measures, which others, situated like the Government of India, must not even dream of. The intelligence of the average Indian peasant is not above believing that the issue of one rupee paper represents the utter exhaustion of all the other financial resources of the Government, and that it is an attempt to quietly deprive the people of their treasured wealth. However much we may deplore such a crudeness it would be sheer madness to ignore it altogether and deprive ourselves deliberately of all weapons to fight it. (4) Those, moreover, are wrong who imagine that a one-rupee note has but to be issued for the rupee coin to flow into the tills of the Banks or the Treasuries of the Government. A five-rupee note gets into circulation because it is easier to carry about than 5 rupee coins. But a one-rupee note would

be in no way be more acceptable than a coin of the like value for the note will be probably larger in size and cumbrous to carry about than the rupee. So long as there is a choice between the one rupee coin on the one hand and a one rupee note, on the other, the average peasant in India is sure to prefer the former. For while the note is a medium of exchange and nothing else, at least in his eyes, a rupee is both a medium of exchange and a store of value. If, thanks to the boom in exports, he is able to accumulate a number of rupees, he can, at a pinch, turn them into anklets for his wife; but so many notes could only serve to light his hukah—and it would be too great a luxury for such as him, if not for those who suggest such a measure. We mention this argument because the notion seems to prevail that the present scarcity in the medium of exchange is due to the fact that the peasant, getting more for his produce now than in former years, is unwilling to part with his hard-won, much beloved rupees in these times of high prices in the ordinary way of purchases for himself and for his family; that he stores up these rupees, and that if he is given notes he would find them easier for storing up than rupees. It is precisely here that the authors of the suggestion under discussion are mistaken. If the peasant really wants to treasure up the rupees, he has, we may be sure, enough sense to prefer bits of silver to bits of paper for this purpose. (5) In spite of all the foregoing arguments however, we would have supported the proposal as a desperate but inevitable measure had we been con-

vinced that there was no other remedy for the present position. It is true, indeed, that the heavy balance of trade in our favour could not be liquidated in the ordinary way by shipping gold to India owing to the prevailing conditions in England whose gold resources have to be husbanded with the most meticulous care in order to maintain her exchange with neutral countries. Since the entry of the United States into the War, and with their promise of a monthly loan to the allies of £ 80 to £ 100 millions, the exchange situation of England—with a monthly excesss of imports over exports of roughly thirty million sterling,—need cause no very grave anxiety. English gold may now be allowed to flow to India to help the present situation. And if the dangers of transport and the chances of total loss on the way make that course impossible, the gold in India in the various reserves may well be issued to tide over the present difficulty. With such possible and practicable alternatives before us we cannot, indeed, support such a risky proposal as the issue of one and two rupee-notes is bound to be at a time like this. (6) And though it is a point of detail only we may mention that even the cost of manufacturing such notes would, in the aggregate, amount to a sufficiently respectable sum as to be serious consideration against such a measure at a time like this.\*

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\*Since the above was written the Government of India have definitely committed themselves to this proposal and we await the results of this experiment.



While, therefore, we desire a greater popularity of the currency notes and their more extensive use than is the case today, we see no means of achieving our object, in the present circumstances of the country, except by universalising gradually notes of Rs. 500, 1000 and even 10000, and offering facilities for the conversion of rupees into notes and vice versa. The development of the cheque system is an alternative impracticable so long as there is only one literate person in a hundred in this country. The issue of one or two rupee-notes, is another alternative, and of a temporary utility, which must not be adopted except in the last instance when it has become absolutely inevitable. The need for elasticity in our system is indispensable; but that, perhaps, would be better secured by recasting the provisions regarding the reserve than by any such measures of momentary value. We shall, accordingly, turn over attention next to the discussion of the Paper Currency Reserve.

#### (b) *Currency Reserve.*

We have already traced the history of this Reserve upto the outbreak of the war, and shown that it consists of two main branches: metallic Reserve and securities, each of which can be further subdivided into gold and silver portions of the metallic Reserve, and Rupee and Sterling portions of the Securities Reserve. On the 31st of March 1914 the Reserve was distributed as follows:—

	In lakhs of Rupees.
Rupees ... ..	20,53
Gold coin and bullion in London ...	9,15
„ „ „ „ „ India ...	22,44
Securities at cost in London... ..	4,00
„ in India ... ..	10,00
<hr/>	
Total ...	66,12.

The composition and the location of the Reserve has aroused much criticism in the past, nor is there any chance of that criticism being set at rest by the recommendations of the Chamberlain Commission on the subject. Taking first the metallic reserve, the introduction of the gold element was originally intended to afford relief to the currency situation in India, but the gold portion has subsequently been used for entirely different purposes. Says the Chamberlain Commission, "The total amount of gold in the Paper Currency Reserve naturally fluctuates inversely with the total stock of rupees in the same reserve. When the rupees threaten to fall short the gold accumulates, and it is by using the excess gold that the cost of silver for fresh coinage is eventually met. As already explained, the authorities endeavour, through the sale of Council Drafts in London, to secure that the gold should not accumulate in India to such an extent as to involve shipment back to London. In practice the amount of gold accumulated in India has, except when depleted by the crisis of 1907-8, always tended to

exceed the maximum demand for gold from the Reserve in India. The policy pursued in quite recent years has been to locate from about five to seven millions sterling in London, and only to secure the presence in London of further gold belonging to this reserve when the money is wanted to purchase silver. This has been criticised by some of the witnesses who appeared before us. It seems to us, however, to be at present justified by two considerations. In the first place it is reasonable that for the purchase of silver some part of the Paper Currency Reserve gold should be kept in London, as the principal source of supply: for this purpose no great amount is required. But, second, there is the maintenance of the exchange to be considered. The facts are that the gold in reserve in India has been much in excess of the demand, that the Gold Standard Reserve has not in itself been sufficient to secure beyond question the stability of exchange, and that gold in London is more directly and indubitably effective for this purpose than gold in India. In these circumstances, so long as the Gold Standard Reserve is insufficient by itself to secure the stability of exchange, we think the policy is justified." This apology is entirely beside the point. The purpose of the metallic portion of the Paper Currency Reserve has always been and must always be the guarantee of converting on demand the currency notes into legal tender money. If in demanding conversion of the notes people in India prefer rupees to gold coin, that is no reason to

consider gold in India as useless. The intrinsic value of the rupee, apart from the abnormally high price of silver prevailing now, is about ten annas, and 16 crores of coined rupees in the Paper Currency Reserve are in reality worth only 10 crores. The introduction of a portion of gold in that Reserve is, therefore, required for giving additional strength to that Reserve. The transfer of a large part of that gold to London, with the object of buying silver for fresh coinage, does not appear justifiable; for the coinage requirements of the Government of India cannot fluctuate so much—they should not be permitted to be so uncertain—as to demand an extra reserve of about 10 crores in England. The suspicion that this gold is kept in London with a view to assist the London money market; that it is a conspiracy to deprive India of its share of the world's gold to which the officers of the Government of India have wilfully lent themselves is likely to gain wide circulation. Moreover the second purpose that this gold is said by the Commission to serve in India is entirely foreign to the original intention of this reserve. If the exchange value of the rupee has to be artificially maintained, the task of that maintenance, should fall on the Gold Standard Reserve and not, under any circumstances, on the Paper Currency Reserve. And if the Gold Standard Reserve is found inadequate to meet all possible demands upon it in the time of a crisis, it is because of the short-sighted policy of gaining interest a substantial portion of that Reserve is invested in securities; it



is because even in that Reserve no adequate gold bullion is allowed to flow to India under the normal course of trade. But whether the Gold Standard Reserve is adequate or not, it is clear beyond the possibility of a doubt, that the Paper Currency Reserve cannot be used for steadying exchange without being false to the purpose of that Reserve, and without placing the Indian currency system in a weak and suspicious condition.

We have not yet mentioned in this connection another purpose which the gold in the Paper Currency Reserve may be made to serve without any violence to the nature and purpose of such a Reserve. The accumulating gold coins may well be used for facilitating the introduction of a gold currency in India. If the rupees were made by law limited legal tender, and if the notes were expressed in terms of gold coins, whether the British sovereigns or any other coin specially minted for India, the advent of a gold Currency as well as a gold standard will be hastened, and that without disturbing in any way the monetary system. The accumulated gold coins or bullion may be first used for the purpose of redeeming the notes in gold when presented, and there is every reason to believe that the people, being used to notes, would accept them all the more willingly when they are made convertible in gold than when they are simply convertible in silver. If the note-issue increases, or even if it remains what it was in normal times, say 70 crores of rupees,

rupees even with a limited legal tender, would be required to the extent of Rs. 100 crores roughly. The total new gold coinage, therefore, taking the currency requirements of India at Rs. 200 crores, would not exceed Rs. 30 crores or £ 20,000,000 at most. But the total gold held in the currency Reserve in India and London amounted in 1913 to Rs. 38.52 crores; so that without having to buy any new gold, we might be able to issue a gold coinage in India more than adequate for all her domestic purposes, and yet leave a considerable margin in the Reserve.

Turning now to the invested portion of the Reserve, we find that the chief ground of attack against the present policy is in connection with that portion of the invested Reserve which is held in sterling securities in London. It cannot be denied that this reserve originates at all because the Indian people have consented to use paper money instead to the extent of the Reserve. It is, therefore, in every sense of the term their money, and the policy which keeps a growing portion of that reserve in the securities of a distant country can have but scant justification on the plea either of abstract justice or statesmanlike prudence. It is, indeed, sometimes alleged that the holdings in the Reserve of other securities, besides those of the Government of India is in perfect accord with one of the most approved maxims of banking. The factors which might cause a run on the Paper Currency are bound to affect, it must be admitted, the securities of the Government

of India. But unless we assume that every note in circulation would be brought for conversion in a time of panic;—unless, that is, we assume that there is no need of any paper currency in India—a manifestly impossible assumption—we have no reason to apprehend that the run on the Paper Currency will be so great as to demand a forced sale of the securities in times of panic. The proportion of the securities held in the Reserve to the total circulation was about 20 per cent; and these will have to be sold only after 80 per cent of the notes in circulation have been cashed and the panic is not yet allayed. This has merely to be mentioned in order to expose its utter absurdity. Moreover the best English securities were bringing only  $2\frac{1}{2}$  per cent and, besides they were steadily depreciating since 1909. The Indian securities on the other hand brought in  $3\frac{1}{2}$  per cent and in spite of all the crisis and famines were fairly steady before the war. And the other contention that the holding of sterling securities is required to strengthen exchange is equally absurd and ill-founded. The object of the Paper Currency Reserve is to guarantee the immediate convertibility of notes on demand. It has, and can have, nothing to do with the maintenance of the Exchange. To confound these two distinct functions of two distinct Reserves, in the hope of strengthening exchange, is to put a heavy strain on each which may prove too much even for both combined.

Another point in the treatment of the invested Reserve, to which attention might be more profita-

bly directed by public criticism, is in connection with the amount to be invested and its proportion to the total circulation. In 1913, as we have seen above, when the gross circulation amounted to 69 crores, the invested portion of the Reserve was only 14 crores or slightly under 20 per cent of the total issue. In 1917 when the total circulation was over 83·40 crores the invested portion of the Reserve was 42·80 crores or over 50 per cent. In 1913 the total active circulation was 45·39 crores so that the invested Reserve was about 30 per cent. In 1917 the net circulation was 80·5 crores and so the invested portion was 55 per cent. and its proportion to the active circulation must be still greater. This vast discrepancy, though caused by the war, would not have occurred if the note-issue were based on more scientific principles. We have shown above that the want of elasticity in our note-circulation can be only remedied by an immediate universalisation of the Rs. 500 notes, and greater facilities for encashment as of right to notes of higher denomination in all circles. But a much better remedy would be to recast altogether: the principles governing our note issue. On this point the Chamberlain Commission recommends "The fiduciary portion of Paper Currency Reserve should be increased at once to 20 crores. But instead of merely fixing this figure as a maximum, we propose that the maximum of the fiduciary portion should be fixed at the amount of the notes held by the Government in the Reserve Treasuries plus one-third of the net circulation for the time being.



Under this proposal the invested portion of the Reserve will be at once increased by six crores. We recommend that this result should be effected by a transfer (at market value) of sterling securities to that amount from the Gold Standard Reserve in exchange for 6 crores of gold now in the Paper Currency Reserve in India." "So long as the gross circulation exceeds 60 crores," they continue, "it will be within the power of the authorities to increase the investments of the Reserve and we propose that Government should have power not only to make such further permanent investments as they think fit, but also to make temporary investments or to grant loans either in India or in London." These recommendations of the Commission are on the whole praiseworthy, and particularly the suggestion about making temporary loans in India. We cannot, however, associate ourselves with the idea of investing a part of these securities in London nor can we endorse the recommendation about short term loans in England. It is, moreover, a great improvement on the present methods, to suggest a combination of the two principles of a fixed maximum reserve in securities, and that of a proportional Reserve. By this means we may legitimately expect an increase in the revenues of India in the shape of the interest for these investments, permanent or temporary, without, however, endangering in the least the convertibility of notes. Moreover, as the currency notes gain in popularity, Government can, by this method, increase either the permanent or

the temporary, or both portions of the invested Reserve without a special act. We need not apprehend any abuse of such a latitude of powers to the Executive since the maximum that can be invested at any moment will be automatically determined by the operation of this principle. For greater prudence sake it might even be suggested that the temporary investments should bear a certain proportion to the permanent reserve, say, 1:2.

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## CHAPTER V.

### **The War and the Indian Currency.**

We have now reviewed in all its aspects the currency organisation of India to-day as it has been evolved and worked between 1899 and 1914. That organisation has been seriously affected by the present war in every detail. In this chapter we shall discuss the effects of the War (1) on the Council Drafts and (2) on the Paper Currency.

#### THE EFFECTS OF THE WAR ON COUNCIL DRAFTS.

The Budget estimates for the year 1914-15 provided a sum of nearly £ 20 million for the Secretary of State's drawings, but on account of the trade depression during the first four months of that year, the demand for Drafts was small. When the political crisis became acute, and when war was declared, trade was disorganised and foreign capital began to be withdrawn from India. The Secretary of State's drawings fell off. The sterling value of the rupee began to go down and a serious break in the exchange was threatened.

The Government, although not bound to give sovereigns for rupees, and, therefore, not bound to prevent the exchange value of the rupees from falling indefinitely, had yet pledged its word to do all in its power to maintain the exchange at 1s. 3½d. Following the recommendation of the Chamberlain Commission, the Government tried to deal with

the situation, first by restricting the issue of sovereigns only to persons or firms wanting at least £10,000 at a time, and later by stopping altogether the issue of gold to private individuals or firms so that the gold reserve might not be unduly depleted. They then offered to sell Reverse Councils at a rate of 1s.  $3\frac{2}{3}$ d. to the extent of one million pounds a week until further notice. Some days later they offered to sell sterling Telegraphic Transfers at 1s.  $3\frac{1}{8}$ d. per rupee. In this way drafts worth about £8·7 million were sold during the financial year. The proceeds of these were credited to the Gold Standard Reserve in India, and the payments made by the Secretary of State in London were debited to the same account in England. Thus in that year the Secretary of State sold Drafts upon India worth about £7·7 million, while he had to pay about £8·7 million on account of Reverse Drafts drawn on him. In other words the novel spectacle of the Secretary of State remitting to India more than the amount received by him by sale of the Council Drafts was seen for the first time. This was really a blessing in disguise because the Government had immediately to face a serious rush on the Post Office Saving Banks, which was met by borrowing temporarily £7 million from the Gold Standard Reserve. The Secretary of State was able to meet his disbursements, (a) by receiving some £8·7 million from the Home Government on account of expenses incurred by the Government of India on behalf of the War Office, (b) by borrowing £10·9 million instead



of £5·9 million as provided in the Budget estimates, and (c) by transferring £1 million from the Paper Currency Reserve in England to his cash balances.

The Budget estimates for 1915-16 provided a sum of £7·1 million for the Secretary of State's drawings. Although exchange was weak during the earlier months of that year, and sterling transfers worth nearly 4·9 million were sold in India, it revived in September 1915, and in the cold weather a strong demand for Council Drafts set in, because, although the war continued, trade adjusted itself to the new conditions. The exports of tea, hides, and jute at high prices were large, while the imports of piece goods, railway plant, machinery, and precious metals were small. Thus there was a strong demand for Council Drafts in that year; and the Secretary of State sold Drafts worth over £20·4 (about 30 crores of rupees). Besides paying this large amount, the Government of India had to incur expenses amounting to £15·6 million (about 23 crores) on behalf of the Home Government and to finance wheat purchases to the extent of about £3 millions (Rs. 4½ crores). In order to meet such heavy demands they took powers to increase the invested portion of the Paper Currency Reserve in England, by means of which about 12½ crores of Rupees were made available in India, by the Secretary of State transferring an equal amount in sovereigns from his Cash Balances to the Paper Currency Reserve and investing it in Treasury Bills.

Besides that a sum of £ 7½ million (Rs. 11¼ Crores) was transferred from the Gold Standard Reserve to the Cash Balances in India, the Secretary of State transferring an equal amount from his Cash Balances to the Gold Standard Reserve. In addition to these methods the Government saved the situation by coining silver heavily. Thus the year 1915-16 passed without any special disturbance in the exchange.

During the next financial year, we find that in the Budget Estimates provision was made for the Secretary of State's drawings to the extent of nearly 5.1 million; as it was expected that he would receive in England nearly £ 18.6 \* million from the Home and the Australian Governments on account of the expenses expected to be incurred in India on their behalf. But on account of large exports of cotton, wheat, hides, seeds, yarns and textile fabrics from India during the first eight months, the demand for Council Drafts was so great that the Secretary of State sold Drafts worth about £ 20 millions from 1st April 1916 to 14th December 1916. In addition to this, Government had to meet heavy expenses\* on behalf of the Home Government. The currency in the country was depleted by the export of large amounts to Mesopotamia, British East Africa and Egypt. In order to meet such large demands upon its Cash Balances, Government took powers to increase still further the invested portion of the Paper Currency Reserve in England as before and

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\* Revised estimate raised it to £ 38½ million.

thus released an equivalent amount from the Paper Currency Reserve in India. It also purchased large quantities of Silver both in England and in India to coin rupees.

However it was found that the demand for drafts would remain heavy while the Treasury balances in India would not be adequate to meet these demands. The Secretary of State, for India in Council therefore, gave notice on the 16th December 1916 that intermediate sales by him of drafts on India would be suspended until further notice, but that tenders for drafts for Rs. 80 lakhs a week would be received on Wednesdays at not less than 1s. 4 $\frac{1}{8}$ d. for bills and 4 $\frac{7}{32}$ d. for Immediate Telegraphic Transfers. It was further added that no allotment to one person or firm would exceed Rs. 10 lakhs in a week.

This announcement caused a good deal of disturbance in Banking and Commercial circles; and, although tenders for amounts larger than those offered on the Wednesday following this announcement were invited, yet these restrictions seem to have produced some important effects. In the first place they caused a stringency in the money market. The principal Exchange Banks, knowing that they were unable to draw funds from their offices in London, were reluctant to make advances freely. Secondly they caused a fall in the prices of many securities, because the persons who were advanced monies against such securities were asked either to pay up their loans or to increase the

margin. Moreover further accommodation against the securities was very much restricted. Thirdly, exports were adversely affected because of the difficulty of financing them. And finally trade in general was suffering from these restrictions.

Various suggestions have been made to relieve the situation. For instance some have suggested a further increase of the invested portion of the Paper Currency Reserve. In order to increase the note circulation, the supporters of this remedy suggest the issue of one or two rupee notes; but such notes are not likely to become popular. Moreover, they will take a long time to displace rupees to any appreciable extent. Even the familiar five rupee notes have displaced only  $2\frac{1}{2}$  crores of rupees according to the figures as they stood on 31st March 1916. Unless the active note circulation increases, the further increase of the invested portion of our Paper Currency Reserve might mean too great a strain on that Reserve. But this point has already been amply discussed in the preceding chapter, and we need not now go over the same ground again.

The two other remedies proposed were:—

1. To allow the import of gold from Japan or America.
2. To release the gold held in the Paper Currency Reserve in India.

Against the first of these it might be said that such import would have an adverse effect upon the Anglo-Japanese or Anglo-American exchange. On



the other hand it might be argued that the adverse effect upon the Exchange would be trivial, while the harm which the restrictions upon the import of gold are likely to do would be considerable. Since America has joined the allies the Anglo-American exchange situation does not occasion so much anxiety as before ; and arrangements have been made recently for an import of gold bullion from these quarters. It is yet too early to say how far this remedy would be effective ; but as far as we can see much more gold would have to be imported if the Exchange situation in India is to be properly maintained.

The second one seems more feasible, because, if the gold held in India in the Paper Currency Reserve is released, an equal amount of it can be earmarked in London by the Secretary of State from the proceeds of the drafts. The release of the gold is very likely to draw rupees and thus strengthen the rupee holdings of the Government. Thus the Secretary of State will be able to sell drafts freely and the situation will be relieved. Hence the Government has taken this step to control the exchange situation.

## II. WAR AND THE PAPER CURRENCY.

The first shock of the great European war in 1914 was a rude but decisive test of the soundness of our Paper Currency system. With the declaration of war the trade in India was paralysed, the Marwari middlemen having fled from Bombay and Calcutta to seek shelter in their remote homes in the hills and fastnesses of Rajputana. The obligations

of the Government of India in London remained the same as ever while exports from India began to fall off. There was a rush at the same time on the Savings Banks deposits as also on the Paper Currency Reserve. Under the circumstances the Government adopted cautious policy to restore public confidence. At first they allowed gold to be issued freely, but when it was discovered that the gold from the Reserve was taken out more by speculators than by persons genuinely anxious about the credit of the Government, they refused, after £ 1 million were thus drained away, to issue any sovereigns at all to private persons. Then there was a rush by timid people on the Savings Bank deposits, which they afterwards wanted to turn into coin; but as Government offered every facility in their power to meet the wishes of such people, the rush never developed into a panic. The depletion of the Savings Banks deposits amounted to £ 7 millions, which, being a floating debt, had to be made good by an equivalent reduction of the current balances at first and afterwards by borrowing gold from the Gold Standard Reserve. The rush to convert notes into coin was strongest where as in Bombay, Burma and the Punjab the credit mechanism was still tingling from the shock of the bank failures of 1913. The net note circulation was reduced by Rs. 7 crores = £ 4½ million.

Owing to the factors mentioned in the first section of this chapter, the demand for the local currency became very urgent in each successive

year of the war. The circulation of notes was therefore increased, and the invested portion of the Paper Currency was steadily increased from 1915. Power was first taken in November 1915 to increase the permissible investments in India by £4 million, and in the early months of 1916 it was decided to make this additional investment in London. Towards March the ordinance of January 1916 was replaced by a Temporary Act IX of 1916, authorising Government to make a total increase in the investments of £8 millions, out of which £4 million were invested in Treasury Bills before 31st March 1916. The total permissible investments at that date were thus £17½ million. The actual investment was Rs. 20 crores, half of which was in England. By notification issued on November 13, 1916, Government took power to increase such investments by another £8 millions, and in December following an equal sum was added to the investments, which were, thus, almost doubled between March and December and raised by 3 times the amount as compared with 1914. It was pointed out that this was necessary because, in spite of the heavy coinage of rupees in 1916, Government were undertaking such heavy expenditure on behalf of the Home Government that their Treasury Balances would not suffice to meet the trade demands for Council Bills. These additional powers were, therefore, taken in the hope that they would suffice to meet the ever-increasing demand.

The position, therefore, on 31st March 1917 was :—

Total Circulation* ... <i>Deduct—Withdrawn from circulation by foreign circles and in course of remittance to circles of issue bil.†</i>	Rs...86,37,51,735	Reserve.	
		Silver Coin (in India)	Rs. 17,10,71,118
		Gold Coin and Bullion (In India) ...	Rs. 11,99,91,932
		Silver Bullion under Coi- nage at Calcutta and Bombay ...	Rs. 1,99,32,772
		Gold Coin and bullion in England ...	Rs. 6,67,50,000
		Silver Bullion in England	Rs. 13,36,772
		Securities (India) ...	Rs. 9,99,99,946
		„ (England)†...	Rs. 38,49,19,195
		Deduct amount due or bills drawn by one circle on another ...	Rs. 2,50,000
	<hr/> Rs...86,37,51,735		<hr/> 86,37,51,735

\* The total circulation went over Rs. 100 crores by August 1917.

† Includes treasury bills purchased under Sec. 3 of Act IX of 1916 at a cost of Rs. 29,99,19,195.



To sum up, then, the effects of the War on the Indian Currency system : The trade of India having improved, and the demands of the India Office having been set off by to the expenses incurred by the Government of India on account of the Imperial Government, there has been an unprecedented demand for Indian Currency to pay the favourable balance of trade in India. This demand was at first met by an unrestricted sale of Council Drafts, but the available stock of rupees was soon exhausted, and all attempts at new coinage were proved inadequate. Incidentally, the great demand for silver has raised enormously its price in gold. When the Councils were found inadequate for the increasing demand the Government had to consider two alternatives viz (1) the import of gold to settle the balance and (2) the extension of the note circulation. As regards the first England as a belligerent was more than ever anxious not to part with her slender stock of gold for exchange purposes ; and it is only since America has come into the War on the side of the Allies, that there has been some slight facility given to the import of gold. We consider this the best and the most effective remedy for our present exchange situation and would be glad to see its extension still further. We need not notice at length the device of transferring the gold belonging to India from one account to another, with a view to its being used temporarily as a remedy of the exchange problem, though even this we would consider a better measure than many other proposals. The

other alternative was an extension of the paper currency. The Government have already committed themselves so far to this policy that we hesitate before pronouncing a definite opinion before we know the results of the new experiments. We think, however, that the policy regarding the extension of the paper currency gives cause for serious reflection.

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## CHAPTER VI.

### **Proposals for a Gold Currency.**

Whatever may have been the predominant metal in the earlier currency of India, it is a matter of history that ever since the consolidation of the system in 1835 by the establishment of a uniform rupee throughout the Company's dominions, the agitation for a gold standard and gold currency has been kept up in one form or another in India. After the revolution of 1835—and when the Company's Government refused to recognise gold coins as legal tender—they were circulating in the country in such abundance that the Government had to withdraw their restrictions within six years of their imposition. In 1852, afraid of too great a depreciation of gold on account of the rapid additions to the stock of gold owing to the new discoveries in Australia and California, Lord Dalhousie's Government once more forbade the receipt of gold coins at the Company's public treasuries, and so gold was completely demonetised as far as India was concerned. But this Notification was certain to meet with an energetic opposition, since it was deliberately running counter to the current of policy of the times. With the returning wave of prosperity in India during the American Civil War, the Chambers of Commerce of the three Presidency cities led the way in the agitation for a gold standard. In 1864 the Government of India proposed, in a dispatch to the Secretary of State, to make sovereigns and half-

sovereigns full legal tender in India at the rate of Rs. 10 = £ 1. They also suggested, in the same dispatch that the currency notes should be made exchangeable for sovereigns as well as for rupees at the above-mentioned rate, though they were not prepared to give the same exchange facilities for gold or silver bullion. The Home authorities were however averse to the suggestion of making the standard English coin unlimited legal tender in India ; but they had no objection to reverting to a state of matters which prevailed in India for many years, namely, that gold coins should be received into the public Treasuries, at a rate to be fixed by the Government, and publicly announced by proclamation. Accordingly a notification issued on November 23, 1864 permitted the receipt of English coins—sovereigns and half-sovereigns—in payment of sums due to the Government at the rate of Rs. 10 = £ 1 and the gold mohurs of 1835 at the rate of 15 rupees to the mohur.

The subject of the Indian system of Currency, however, after having been the victim of four or five radical changes within a period of less than 30 years, was sure to be considered sufficiently muddled as to require the enlightening inquiries and advice of a Royal Commission. The year 1866-67 witnessed the sittings of the first of these Commissions, who found that the demand for gold currency was unanimous in the country and recommended that English and Australian sovereigns be accepted at the specified rate at the Government Treasuries, and that the currency notes be issued in exchange for gold. The



first recommendation was adopted in 1869 with the slight modifications of a rise in the value of gold, the sovereign being now valued at Rs. 10-4.

This was on the eve of the Franco-Prussian War and the subsequent demonetisation of silver by Germany. Within three years after this change Sir Richard Temple, the Finance Minister of Lord Northbrook's Council, presented a long and well-thought out memorandum advocating a gold standard and a gold currency for India. During the anxious years that followed, suggestions were more than once put forward by the Government of India; but the Home Government refused to accede to them. We have already narrated the events which led to the appointment of the Fowler Committee and detailed the events and measures which were adopted in consequence of the closing of the Indian Mints to the free coinage of silver. But we may note here the pronouncements of some of the highest Indian authorities on the necessity of a gold currency for India, before examining critically the whole situation in detail. Sir James Meston, the then Financial secretary, now Lieutenant-Governor of the United Provinces, declared in his speech on the Budget in 1910. "The broad lines of our action and our objects are clear and un-mistakable, and there has been no great or fundamental sacrifice of consistency in progress towards our ideal. Since the Fowler Committee that progress has been real and unbroken. There is still one great step forward before the ideal can be reached. We have linked India with the gold countries

of the world, we have reached a gold exchange standard which we are steadily developing and improving. *The next and final step is a true gold currency. That, I have every hope, will come in time, but we cannot force it.* The backwardness of our banking arrangements, the habits and suspicions of people, the infancy of co-operation-all stand in the way. But the final step will come when the country is ripe for it." And the same views were expressed by the Government of India in a dispatch to the Secretary of State dated May 16, 1912. "It is, we think, an undisputed fact that the establishment of a gold currency was regarded as the logical and natural sequence of the closing of the mints to silver, and as the necessary accompaniment of the establishment of a gold standard. Such a measure will mark a step along the path which has been authoritatively accepted as the line on which our Currency policy must develop, and in time it will be of great assistance in maintaining the stability of our Currency system. Our proposal for a gold coinage has behind it the overwhelming support of the Indian public opinion."

The Government of India at first suggested, following the recommendations of the Fowler Committee, that the English standard coins--sovereigns and half-sovereigns should be minted in India. To these the Home authorities made several objections. If the Indian mints were to coin English coins, they must be branches of the Royal mint and work under its regulations-which

was not practicable. And if the Indian mints were made an independent body the mere establishment would be too costly to permit a free coinage of gold in India. The Secretary of State then suggested to the Government of India (Dispatch dated October 18, 1912) that instead of sovereigns, Indian gold coins of the denomination of Rs. 10 should be coined in Bombay, and the Government of India, rather than forego their proposals altogether, accepted even this costly alternative. This, too, was frustrated by the opposition of the British Treasury, and the Government had at last recourse to the appointment of a Royal Commission-the fourth of its kind within less than sixty years-to inquire into the entire system of Indian currency and report upon the same.

The Chamberlain Commission has come to the conclusion that "It is not to India's interest that further efforts be made to encourage the circulation of gold as currency. We regard gold in circulation as wasteful, and we think that India should be encouraged to develop economic habits in matters of currency. But while educating the people of India in the use of more economic forms of currency, it is important that Government should continue to act on the principle of giving the people the form of currency which they ask." In these words they have given their benediction to the *status quo*, and for all we can see at present, the artificial currency of India has come to stay under the style of a most scientific system and with the blessings of eminent theorists on the subject.



Let us, however, examine in some detail the arguments in favour of the present system of a token currency for internal purposes, and gold stored up in reserve for the purpose of maintaining the Exchange. (1) In the first place it is claimed that if we had an actual gold currency, we would find it very difficult to find the necessary quantity of gold for export in the event of a serious financial crisis. For gold in circulation, it is urged, will, in times of crisis, be hoarded by the people instead of being brought to the banks for easing the exchange situation. And if even the educated people of Western Europe are prone to such short-sighted conduct in the event of a crisis, what shall we say of the people of India with their centuries old habits of hoarding? It is further added that the example of countries like England with an actual gold currency should not be taken as a model by the currency reformers in India. England is normally a creditor country, and she can, therefore, tide over any ordinary crisis by simply contracting her loans to foreign borrowers. This she frequently does by means of her single centralised gold Reserve at the Bank of England, and that institution, by raising sharply its rate of discount, may place a practical embargo for a time on foreign loans. Besides, the development of the cheque system in England has rendered the metallic currency and even the Paper Currency a matter of altogether secondary importance. In all these respects India is at the antipodes as compared to England. She is habitually a borrower while



England is habitually a lending country ; 90 per cent of her population is illiterate and they cannot therefore understand the importance of representative money like notes, and much less of cheques ; in England every man in business has a banking account, and banking therefore, has made vast strides there, while banking enterprise is yet in its infancy in India.

(2). Secondly the people of India do not need a gold coin. For any gold coin which is at all convenient to handle, would be too large for their ordinary payments. In illustration it is pointed out that the Government made an attempt in 1900-1902 to put sovereigns in circulation, but as after a short time the bulk of them were returned to the Treasuries, it is fair to assume that, allowing for the melting operations of the bullion dealers, very few sovereigns would have remained in active circulation.

(3). Thirdly if India were to institute her currency system *de novo* on the basis of a Gold Standard and a gold currency she would find it very hard to get the necessary gold. For she herself does not produce gold at all adequate to her own needs. And if she were to purchase fresh gold from the existing stock of the world, by means of the rupees, the price of gold in terms of silver would be suddenly forced up, and India would have to sustain a heavy loss for a purely sentimental reason...

These arguments, we must observe, are none of our own fabrication, but are practically those given

by the most brilliant exponent of the Gold Exchange Standard and the champion of the present system in India, Prof. J. M. Keynes. Any one who reads his book on Indian Currency and Finance cannot fail to trace a close affinity between his line of reasoning and that adopted by the Chamberlain Commission; and the three chief arguments in favour of the present system as summarised above may be found equally in the pages of the report of the Royal Commission on Indian Currency and Finance (1913) or of Prof. Keynes' Indian Currency and Finance.

Let us now take these arguments seriatim. The first one is based on a misconception of India's position in international commerce. Though she borrows heavily every year, she is not a debtor country in the sense that the annual balance of trade is generally against her. Even after paying her heavy annual burden of the Home Charges she has almost always managed to retain a considerable surplus of exports of her produce over the imports. The fear of a financial crisis is, therefore, wholesome, but apt to be exaggerated in the case of India. If we take the figures of the last 30 years, including two great wars, two great famines, and several minor occasions for stringency, we would find that not even once did her exports at all fall below her imports. Only if we deduct the amount of Home Charges from the balance of trade she was required once or twice to export precious metals to make up that deficiency. While, therefore, we may admit that India is, for many

reasons, at the antipodes of England, and that consequently England is the worst possible model for us in matters of currency, we must maintain that at least in respect of an international drain of gold India would be in as good a position as England in any conceivable crisis. The fact that during three years of the greatest war on record she has been able to meet all demands upon her from her own resources, besides contributing heavily to the cause of the Empire, would have alone sufficed to show that India would in any year have ample gold resources in spite of the proverbial hoarding propensities of her people to meet all claims against her. It is not unreasonable to assume that if once in ten years the balance after taking the Home Charges into account goes against her the gold Reserves belonging to the Paper Currency, the Gold Standard Reserve as well as the gold in the Government Treasuries would be enough for the purpose. And if unfavourable conditions continue for more than one year in succession—a very rare occurrence, indeed, she can at the worst borrow abroad to maintain her credit. Besides, even if we admit that the people of India would hoard gold which is in circulation, we must not forget that such hoards will never be beyond what the people can reasonably spare. It is not quite consistent to say in one and the same breath that the people of India are too poor to use a gold coin, and that they will store up gold. If 80 per cent of the population can barely get the necessaries of life,



surely they cannot be deemed guilty of hoarding gold for the simple reason that they will never be able to possess a gold coin-even one of the lowest denomination. A very small number of bullion dealers may, it is true, hoard up enough to account for the entire population. But even they cannot hoard beyond their ability. If in normal times there is a favourable net balance of between £ 15 to £ 25 million, which is paid largely in gold, all that gold could not be taken up and hoarded by the bullion dealers or the general public. Almost certainly a considerable portion will return to the Banks or the Government Treasuries, and there will, therefore, be always an adequate Reserve to meet all possible demands of international balance of accounts. Lastly, the remedy for this apprehension of a scarcity of gold in times of financial crisis, is not to have an artificial currency which requires a ceaseless watching and constant managing, but a better banking system which would always guarantee the payment of the country's foreign obligations. Banking in India is admittedly in its infancy ; and a proper development of it would go much farther in assuring our solvency in international indebtedness than any system of managed, " scientific " currency.

As regards the second argument the following table from Prof. Keynes is a sufficient refutation. Though he tries to explain away this damaging evidence from official records we shall see that the answer is indeed unanswerable.



Year.	Net addition to stock of gold <i>i. e.</i> imports exports production. 1=(2)+(3)	Net addition of gold in P. C. Reserve and Treasuries. 2	Net addition to stock of gold in public hands 3=(4)+(5).	Net addition of gold bullion in public hands. 4	Net addition of sovereigns in public hands. 5
	£	£	£	£	£
1901-2	3,223,000	5000	3,228,000	2,261,000	967,000
1902-3	7,882,000	2,870,000	5,012,000	2,814,000	2,198,000
1903-4	8,963,000	944,000	8,019,000	4,741,000	3,278,000
1904-5	8,841,000	38,000	8,803,000	5,866,000	2,937,000
1905-6	2,698,000	6,840,000	9,538,000	5,806,000	3,732,000
1906-7	12,061,000	193,000	12,254,000	7,098,000	5,156,000
1907-8	13,677,000	993,000	14,670,000	7,243,000	7,427,000
1908-9	5,022,000	2,843,000	7,865,000	4,422,000	3,443,000
1909-10	16,620,000	6,347,000	10,273,000	7,407,000	2,866,000
1910-11	18,153,000	71,000	18,082,000	9,991,000	8,091,000
1911-12	27,345,000	9,347,000	17,998,000	9,117,000	8,881,000
1912-13	24,551,000	4,231,000	20,320,000	9,320,000	11,000,000
Total	149,036,000	12,974,000	136,062,000	76,084,000	59,976,000

Thus out of £ 149 millions absorbed by India in the last 12 years nearly £ 136 millions or more than 90 per cent was taken up by public. Out of these less than £ 60 millions or about 44 per cent ( or 40 per cent of the total ) were in coined money, and the remaining 56 per cent were in bullion. Against this the experience of a single year, when £ 6,750,000 were put into circulation out of which about half were returned to the Government, can hardly be pleaded with propriety to show that gold money is not wanted for the purposes of circulation in India. However vast may be the operations of gold-exporters and professional bullion dealers, we cannot imagine that they have succeeded in exporting any substantial portion of the gold coins in India. In fact a creditable estimate of the total currency in India shows that out of a total currency of Rs. 300 crores in circulation in 1914, the rupees amounted to Rs. 180 crores, the notes amounted to 60 crores and the rest was represented by gold coin in circulation. If we accept this figure, over  $\frac{2}{3}$  of the gold coins imported were in circulation before the war. But this estimate, there is reason to believe, understates, rather than over-states the number and value of the gold coins in circulation.

The last argument against the establishment of a gold currency in India is also answered by the tables given above. Even though India's home production of gold is very little being a little over £ 2,100,000 a year, India can rely on a steady flow of gold to her owing to her favourable balance of trade,

Within the first twelve years of the century, if the Government of India were minting their own gold coins, they could have put at least £100 million worth of coins in circulation, besides retaining in their own hands a Reserve of £50 millions in their Paper Currency Reserve and Treasury Balances. And all that could have been done without having had to purchase gold by our superabundant silver, and consequently at a great loss to the country. The adoption of a Gold Currency would not have required in 1900—any more than in 1920.—the immediate conversion in gold of every rupee and note in circulation. A large number of the rupees about 100 crores must necessarily remain in circulation as also about Rs. 50 crores worth of notes. We would require, therefore, about £50 million of gold coins to bring about a gold currency; and if that amount is spread over 5 years—during which rupees may remain legal tender and afterwards they may be reduced to the position of token coins—our ordinary excess of exports would more than suffice to bring in the required gold.

The positive arguments in favour of a gold currency in India have been thus enumerated by the Chamberlain Commission. “(1) That gold is a more convenient and portable medium of circulation than the rupee; (2) that a gold currency is a necessary step towards what may be regarded as the ideal currency, viz., paper backed by gold in reserve; (3) that some prestige attaches to the possession of

a gold currency whereas a silver circulation is the mark of a less progressive peoples ; (4) that a large amount of gold in circulation is a strong, and, in the view of some people, the only adequate support for exchange ; (5) that the constant mintage of fresh supplies of rupees is objectionable, and would be obviated by an increasing circulation of sovereigns ; (6) that until India has a gold currency in active circulation, India will continue to possess an artificial and managed currency ; (7) That India should be encouraged to absorb gold in order to protect the world in general from a further rise of prices due to the greatly increased production of gold.... ”

As may be expected the Commission tries to meet all these arguments ; but their answers are hardly convincing. Thus on the first point they bring forward the time-honoured statement that for the small amounts of the average Indian transactions gold can never be a more convenient medium than silver. This, however, does not deny the fact that for the larger payments gold is more suitable. On the second point they appeal to history and find no example of a country which got a good paper currency only after it had established a gold currency. “ A paper currency ” they say, “ if readily encashable is the most convenient medium of circulation.” But they omit to state that the note being a form of money which circulates at all because there is general confidence in the issuing authority ; that authority would be guilty



of want of faith if they cash those notes in anything which gives the holder less than the face value. Ever since the day that the legal value of the rupee was divorced from its bullion value, the notes, when converted in rupees, would bring much less than their real value. Even, therefore, if paper currency is the most convenient form of medium of circulation, the dictates of commercial honesty require that they be converted in the kind of the metallic money which retains its value most steadily. Both these arguments are, therefore unanswerable. As regards the third argument the Commission distinguish between a gold standard, to which they admit some prestige does attach, and gold currency in the sense of a prepondering use of gold for internal purpose; and they go on to say that no highly civilised country now a days uses an important amount of gold in their daily transactions as compared to other forms of money. As far as this argument shows a craving for imitation we have no sympathy with it; but in so far as it shows that for purposes of international trade a gold currency carries greater importance, we regard it as a strong argument. But it is the fourth point to which the Commission seem to attach the greatest importance. Even here they try to show that a mere gold currency in a country is no guarantee of its international obligations being always met with promptness, which really depends on banking Reserves. Moreover if the gold currency in India is intended to be of the same dimensions as that pre-

vailing in Egypt, no doubt India would have sovereigns to spare for export in time of depression ; but this would mean a great displacement from currency not only of rupees but also of notes, and to displace any part of notes will not be to India's advantage. If, however, "the Commission go on to say," the advocates of a gold currency contemplate only such an addition of gold to the currency as can be made through the gradual increase of the aggregate circulation, without detriment to the existing circulation, of notes or withdrawal of rupees now circulating, gold must continue to occupy for a good many years to come no more than a subsidiary position in the currency system. We do not believe that exchange would materially benefit from the circulation of gold on this scale." To this reasoning of the Commission there is an obvious reply. If the maintenance of exchange in any country is secured in the last resource not by the kind of currency in circulation, but by the banking reserves in the country, then that is an argument not for crying down the need for a gold currency in India, but rather for laying a stress on the necessity of developing further our banking enterprise. Besides, the assumption is altogether unfounded that the kind of currency in circulation does not in the last instance act as the support of exchange ; the banking reserves themselves depend—they must depend on the kind of currency in circulation. To ask the banks to have a reserve in bullion of coined gold while the currency in the country is silver is to ask of them a

deliberate confusion in accounts, or to put a premium on banking dishonesty. And as to the other aspect of the Commission's reasoning, if gold currency is introduced, it would, if at all, displace only the rupees. Supposing a gold coin in circulation of the value of Rs. 10, notes of only Rs. 5. and Rs. 10, if at all, would be displaced; all the other notes of higher denomination, being more convenient than gold, must remain in circulation. And even the displaced five-rupee and ten-rupee notes could be more than replaced by a new issue of 20 twenty rupee notes. With the introduction of a gold currency in circulation, notes will be expressed in terms of the new gold coins; and notes being convertible into gold, the note-circulation will rather increase than diminish. Nor will the rupees be displaced to a very great extent, since they will be needed for small change. Gold put in circulation will therefore represent a net addition to the country's currency which will, however, very soon be absorbed by the growing needs of the community for currency. Without, therefore, displacing either notes or silver, without, that is, depriving India of any considerable portion of the more economic forms of currency, we would still have gold in a sufficiently large quantity to be of material assistance to exchange in its hour of need. The coinage of the token rupees would then have to be either entirely suspended or considerably restricted. Their legal tender would be concurrently limited. Given those two conditions the remark of the Commission that,

"all experience goes to show that, so long as the public have the option of making payments in tokens or in gold, it is the surplus tokens and not the gold which will seek an outlet at a time of weak exchange" would have no meaning, since there would be neither an option in making payments, nor surplus tokens in circulation.

We need not discuss at length the Commission's argument against weakening the Gold Standard Reserve for introducing a gold currency in India. For that Reserve was created in order to support exchange while the currency in India consisted of rupees; and it was meant to facilitate the advent of a gold currency, as it was built up out of the profits of coinage, that is to say, from the surplus which arose on account of giving the people of India less in coins than their goods or services were worth. With a gold currency in circulation we would not need at all any Gold Standard Reserve, and the argument would have been ignored as fatuous but for the respect which the array of talents and experience in the Chamberlain Commission could boast of. The remaining arguments in support of a Gold Currency in India are in one way or another connected with the preceding arguments, and we need not, therefore examine at length the answers of the Commission to them.

In all these arguments, however, sufficient importance has not been given to what we consider to be the strongest argument for a gold currency. A



gold currency in India would mean a much steadier level of prices. It was, indeed, suggested to the Commission that with the absorption of gold in India the world in general would benefit. But the Commission brushed that argument aside, with the remark, "The extent to which India should use gold must, in our opinion, be decided solely in accordance with India's own needs and wishes, and it appears to us as unjust to force gold coins into circulation in India, on the ground that such action would benefit the gold-using countries of the rest of the world, as it would be to attempt to refuse to India facilities for obtaining gold in order to prevent what adherents of the opposite school have called the drain of gold to India." It cannot, however, be denied that with the increasing annual output of gold in the world, the price-level would necessarily rise, unless additional uses for gold may be devised. The increasing absorption by India would be one of such uses. No one, of course, proposes that India can, or should be made to, absorb more than she needs; but the Commission seem to be strangely oblivious of the fact that for the last 17 years at least India has not been permitted to take all the gold she could conveniently absorb, by the unlimited sale of Council drafts. Moreover, if India had a gold currency, the risks of depreciation to capital investment in the country would disappear, and more capital will flow to India for the development of her new industries. Again, with a gold currency in India there would be no occasion, to retain, as is now the custom, such large

amounts of India's money in the shape of cash balances and the Reserves in England. All that money would remain in India, and it would be used, either to reduce the burden of taxation in India, or to promote her material development whether directly by Government Agency, or indirectly by means of assistance to trade in general.

All these reasons must have made it clear to the reader that the currency system of India needs remodelling. That in the course of this War India has been able to meet all obligations without any recourse to such exceptional measures as a moratorium or closing the stock exchange, is due not to the excellence of her currency system but to the peculiar circumstances whereby the War, instead of causing a dislocation of her trade and industry, has given her the most hearty stimulus. We dare not think what would have been India's position if she were placed in the same situation as England has been, with a monthly excess of imports of nearly £ 30 million. She has no gold to speak of certainly not enough to right such a fearfully adverse exchange situation—even if it had lasted for a single year. Her people are too poor to have securities of other countries, and she cannot therefore fall back upon—as England did—mobilising foreign securities to correct or steady the exchange. Within the country itself the token currency, in stead of being in increasing demand as it now is, would have been knocked down, owing to want of confidence. We could not

have depended even on borrowing abroad, as we would have hardly been trusted. It is lucky that this war did not force a moratorium in India; but if it had, our national bankruptcy would have been as prolonged as it would have been humiliating, and there would have been no easy recovery for us.

In the face of these lessons it would have been the height of fatuous self-complacency to congratulate ourselves on having escaped the danger. Our currency system needs remodelling—and that on the lines of a gold standard and gold currency. We have already suggested in the preceding pages how this can be accomplished with the least disorganisation, and in the appendix to this work we have given a draft of a bill overhauling the whole system and introducing a gold standard. The principle underlying those proposals is to make our notes convertible—at the end of the War—into gold coins, either the English sovereigns or a specially minted new gold coin of smaller denomination for India. The rupee with its subdivisions may remain in circulation as before; only it must be made a limited legal tender—say for sums not exceeding Rs. 50—to which extent it might be given in exchange even for notes. But the notes should be expressed in gold. To accomplish this we need gold to the extent of about  $\frac{3}{4}$  of the total notes in circulation as a reserve to secure immediate convertibility of notes, and as much again at the most for the ordinary currency purposes. Now if we assume that our normal

note circulation is about Rs. 60 crores, we would, according to this calculation, need at the most about Rs. 80 crores in gold or £ 54 million. But our existing metallic Reserve against Paper Currency and the Gold Standard Reserve would together be more than enough to meet all our needs. The metallic portion of the Paper Currency Reserve may simply be kept in gold as it is, and the Gold Standard Reserve, converted into bullion, may be used for the purposes of coinage. All subsequent readjustment should, of course, be left to be determined by future experience. As regards coining gold it would be preferable, even at some cost, to have our gold coined at the Indian mints—which need not, therefore, work as branches of the Royal mint. If these suggestions were adopted, we feel confident our currency system would be as scientific as it would be popular.

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# **PART II.**

## **BANKING.**

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### **CHAPTER I.**

#### **Some General Principles of Banking.**

##### **I. ORIGIN OF BANKS.**

Historians of the social sciences are not yet agreed about the precise date and mode of the origin of banking business. If we think only of the present day banks and their operations; if we regard only those concerns as banking concerns proper which finance a country's industry, which liquidate its international indebtedness, which manipulate its currency organisation, we would most likely imagine a very short history; for like most other social institutions banking business has grown very slowly, and assumed all its present functions at no remote date in the past. The etymology of the word "Bank" suggests an origin which would not trace the history of banking in Europe beyond the Middle Ages. The term "Bank" is variously derived from "Banc" or bench upon which the medieval

European money-lender and money-changer was wont to lay out his stock and ply his trade; or from "Bank" the German term for a Joint-Stock fund, which was converted by the Italians into Banco or the accumulation of money or stock. In either case we would have to date the origin of banking in western countries not before the period when the great commercial towns of Italy—Venice, Genoa, Pisa—were at the Zenith of their greatness. It is, however, a fact of history that banking business in some form must have been known in the days far, far anterior to the domination of the European commercial world by the merchant princes of Italy. If we regard manipulation of credit as the essence of banking business we find banking operations being carried on in India, Chaldea and China, centuries before Greece had perfected her scheme of social organisation, set a model and compelled an imitation by her Roman conquerors and their barbarian successors. The Institutes of Manu\* are full of regulations about

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**\* Chapter VIII.**

§ 140. A money lender to increase his capital may take the interest declared (legal) by Vasistha, (namely) an eightieth part of one hundred per month (15 p. c.)

§ 143. But he may not increase his capital by taking interest if a pledge has been given him of which he has free use; nor he may dispose of or sell the pledge, although ( it has been in his possession ) for a long time.

§ 151. Interest on money, if all paid at once and at the same time into ( as the debt ), should not be more than enough to double (the principal) and ( the sum of the interest and principal ) should not be more than five times (the principal, when this interest is paid ) on corn, fruit, wool or draught animals.

credit and the rate of interest. In Assyria they used the instruments of credit even before the advent of official coinage\* Both in Athens and Rome the banker's calling and position were publicly recognised. If the silver drachma of Athens were acceptable everywhere as Xenophon says, while those of other Greek cities were current only within their own jurisdictions, it was because the Athenian banker had already learnt the value of money in trade and industry, and could, therefore, receive deposits on interest and lend them out again at a much higher rate. So important in fact was his business that it was subject to strict official regulation. Rome copied these regulations when her "Argentarii" became as important as those of Athens, and compelled them to keep at least 3 books, a cash-book, a day-book and a deposits-book, the books and accounts to be produced for inspection by public officers whenever desired.

This rise of credit instruments is, naturally, almost coeval with the rise of banking. Once it was found that the banker could benefit himself as well as the community by collecting in his own hands the idle wealth of the country to be employed by him in the most profitable manner, it was only a question of time for a bold and ingenious banker to devise means for increasing apparently that

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\* Cruchon *Les Banques dan l'antiquite*'.

wealth even when in reality it remained the same. The Athenian and Egyptian bankers, at first mere money-changers, in course of time understood, created, and used instruments of commercial credit, long before the medieval banker in Europe had perfected his Bill of Exchange. Even in our own country, the Hoondi, though no one can date its origin precisely, appears to be of at least as great an antiquity as the Bill of Exchange.

The European banks as we now know them are indebted for their origin to the enterprise of the Jews. For a variety of reasons this despised but industrious race was obliged to assume and monopolise the functions of bankers in the Middle Ages. Almost all the countries of the Christian world agreed in excluding the Jews from the rights and duties of proprietors of land, and so the Jews were under a peculiar necessity of having all their possessions in a liquid form. The constant dread of confiscation sharpened their ingenuity in devising instruments for the rapid and secret transfer of their property, and hence the development and perfection of the Bill of Exchange which even now remains a credit instrument par excellence. Devised originally as a measure of self-defence, this bill of Exchange was soon converted into an instrument of profit whereby the Jews facilitated the international trade of Europe in the Middle Ages and dominated its industry. For by the strict rigor of the Canon Law



the Christian was forbidden to lend money at interest, and so the Jew became the financier alike of the Knight and Baron going on a crusade and of the merchant embarking on a new venture. The Jews were excluded from all the guilds in Christendom, but by this means they formed a guild of their own, all the more powerful as it came to dominate all the other guilds. And as they had better chances to trade in Christian lands than Moslems, and still better in Moslem lands than Christians, the expansion of commerce on all the shores of the Mediterranean was a source of gain to the Jews.

It was long before the real causes of Jewish supremacy in Medieval Europe were discerned; and because the discovery involved a humiliating admission for the Christian the steps taken to wrest that supremacy were slow and half-hearted. As early as the thirteenth century, Albert le Grand declared that "if usury is against the perfection Christian law, it is at least not contrary to civic interests".\* And St. Thomas Aquinas admits that the lender suffered a loss by making a loan for which he ought to be in justice compensated. The word "interest" was thus coined to take the place, and avoid the consequences, of the hateful "Usury". With the authority of this great medieval sociologist to back them, European legislators began to permit interest at a reasonable rate on Bills of Exchange, which, they required, must be drawn by a person in one state upon a person in

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\* Conant: Principles of Banking.

another state. Soon after "the Bill of Exchange" was converted into a form of direct loan, called the "dry exchange" by which the borrower drew a bill on some fictitious person in some foreign town at the current rate of exchange, which he delivered to the lender. At maturity the bill was returned protested and the borrower charged with re-exchange and incidental expenses. And the transition was completed when the Italian bankers received available cash in the name of deposits to be used in their own commercial and financial transactions. Says Conant, "Thus gradually arose from the need for them all the attributes of modern banking. The individual money-changer, the Jewish money-lender, the Lombard banker, gradually gave way, as centralisation advanced in commerce and in national life, to public banks doing business under official authority."

The modern banks proper, then, may be said to date from the close of the Middle Ages. They were allowed to receive deposits, facilitate exchanges, make loans to the state and private individuals. The oldest bank of somewhat modern type was the Bank of Amsterdam founded in 1609. The Dutch currency at the time was very defective, with a large quantity of clipped coin in circulation. Full weight coins were scarce and at a premium. The city authorities thought the evil was due to the dealings of money-changers and bankers, and so, by decrees issued in 1608 and 1609 they abolished all money-changers and bankers, and established their own Bank in 1609 to

serve as a money-changing and banking institution combined.\* The Bank of England, which followed in 1694, had its origin in the necessities of the state requiring large sums to finance its perennial wars. And though Swedish Banks were issuing notes since 1658, the Bank of England was the first great official Bank which was privileged to issue notes. This was no monopoly of the Bank of England; but since in 1708 a law was passed to prohibit the issue of notes by any other corporation of more than 6 persons, the position of the Bank of England became unique. The first bank of issue in France was established by John Law in 1716, was made the Government Bank—the Banque Royale—in 1718, and failed soon after. To attempt a historical sketch of banks even in the leading countries would be beyond the scope of this work; but these few facts are given to show the origin and development of Banks in the modern world.

It is impossible to trace the development of banking in India; partly for want of historical material and partly owing to the combination of the functions of a merchant and banker in the same hands. As already remarked the phenomenon of loans of money on interest seems to have been well understood in ancient India as the laws of Manu and the precepts of Chanakya alike testify. But the subsequent development shows little trace of a clear, separate development of banking busi-

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\* The city of Hamburg followed suit and had its own Bank in 1619 and the Bank of Stockholm was founded in 1668.

ness in India in aid of all other businesses, but independent of them. Thanks to her medley of independent principalities and her growing foreign trade, India must have needed, long before the commencement of the Christian era, the services of money changers and money lenders. But the men who dealt in money-changing in this country, the men who evolved the Indian Bill of Exchange—the famous Hoondy, which is an instrument for borrowing as well as for transmitting money from place to place, independent of any sale of goods,—carried on at the same time the functions of a merchant or even of a revenue-farmer. The shroff as such was not unknown; and the profits of his business must have been not insignificant. But the conditions of the country prevented the growth of an independent class of business men who dealt in the wealth of others.

## II.—BANKING AND INDUSTRIAL EFFICIENCY.

At the present moment it would be an unquestioned truism of economic science to urge that the industrial efficiency of a country is conditioned by the development of banking in that land. The progress we have already made in commerce would have been impossible without the development of the modern means of communications. And, but for the developement of credit and credit instruments as put forth by the banks, the growth of our world-wide commerce and our gigantic industrial undertakings would have been inconceivable. To appreciate



the importance of banking in modern society, the sketch we have already given incidentally of the functions of bankers is not enough; and we shall, therefore, proceed to attempt a more connected and coherent account of the recognised functions of banks to-day.

### III.—FUNCTIONS OF THE BANKER.

As already noticed the causes which led to the origin of banking were connected with the foreign trade of a country, and consequently the oldest functions of a banker are those of money-changing and foreign exchanges. Even to-day these are by no means unimportant; but with the growth of business and enterprise, new functions have been undertaken by banks which collectively help to give all the facilities that the industrial society now expects from its bankers. We may class these functions, for the sake of convenience as:—

- (1) Borrowing and lending money.
- (2) Dealing in exchanges, foreign and domestic, including transmission of money from place to place.
- (3) Serving as Government Agents in matters financial.
- (4) Issuing Paper Money.

#### I. DEPOSITS AND LOANS.

This is one of the earliest functions of banking houses, and still remains one of the most important.

The banker finds it impossible to carry on his business—on the scale on which it is now conducted—with his own money *i. e.* with the capital invested by himself or by the share-holders. The vast business premises now required for housing a banking business would alone eat up a large portion of such capital. It is with the borrowed money of other people that he conducts his world-wide operations; and the cynical definition of business as other people's money becomes in his case at least a universally acclaimed reality. The question how to attract this money is, therefore, the most absorbing for a banker. In days gone by when the order maintained in a state was not so perfect as we are now accustomed to from all civilized governments, the bankers of Italy, Holland and England used to receive deposits from people, who could not guard their own wealth as they would desire, on condition that the depositors should pay a certain sum—perhaps a certain percentage—to the banker for taking care of their money. But times have now changed. The banker, like every other businessman, is able to earn interest on every penny that he can conveniently spare; and so instead of asking for some remuneration for taking care of other people's money, he is only too willing to give something to the depositors for allowing him the use of their money during their convenience.

Even thus the banker is at some disadvantage compared to other agencies in the same market which are bidding for other people's money. Since

the essence of banking business consists of obtaining liquid wealth on as easy terms as possible, and lending the same wealth out on the best terms obtainable, he cannot afford to pay interest on deposits at a rate which would leave him no margin of profit. The other borrowers of other people's money—the Government, the local bodies, the industrial entrepreneurs or the spendthrifts—are able or willing to offer much better terms than the banker can ever afford to suggest; and he, therefore, cannot attract all the money with which he carries on his business in the shape of bonds, or debentures, or stocks. The fund from which he derives his deposits is made up of the coins or idle money in the pockets of the people; and the way in which he induces them to part with their money is by offering certain services in return, which the other borrowers cannot offer, in addition to a small percentage of interest. The deposits of an ordinary commercial bank, therefore, consist largely of (a) the floating cash in the hands of the clients of the bank, (b) obtained by the banker for custody and use during the convenience of the customers, (c) in return for certain services agreed to be performed by the bank on behalf of the customers, (d) over and above a small rate of interest.

In this definition of a bank's deposits two or three points require more than a passing mention. (1) The services agreed to be performed by the banker consist usually of acting as the paymaster and accountant of the customer. Out of the monies

deposited with the banker the customer may go on ordering the bank—by means of a cheque—to make payments to his tradesmen or for his purchases either for immediate consumption or for industrial employment. Similarly the monies due to the customer from time to time would be collected by the banker, whether in the shape of salary bills, professional fees, sale proceeds of his manufactures, or dividend warrants or bond coupons. All these receipts and payments on behalf of the client the banker immediately notes down in his various books, and periodically copies them—with the necessary changes in the sides of the account—in the customer's pass-book. The customer is thereby spared all the worry of collecting his income, and defraying his expenses item by item, and keeping regular accounts of the same. And the banker, too, finds no great loss in this, as he has to perform the same service for a number of customers, and can, therefore, do so at much less expense than the customers would have to undergo. The banker by concentrating and organising his business can manage the whole of it with fifty clerks, while the same volume of business conducted by each customer on his own account would require perhaps a thousand clerks or more. It is, therefore, mutually beneficial. As a rule the banker makes no charge for these services, the theory being that the low rate of interest he gives on deposits in the current account is enough to make up for the expense he thus incurs. (2) The rate of interest, though low on all deposits compared to



the general rate in the market, differs according to the nature of these deposits. Deposits in current accounts, usually receive the lowest rate of interest, while some banks, like the Bank of England, or the Bank of France, give no interest at all on these deposits. Deposits for a fixed period of six months or a year receive a slightly higher rate, since the banker has greater liberty in employing these. In England the practice of the Joint Stock Banks is to allow on deposits interest at a rate  $1\frac{1}{2}$  per cent. lower than the Bank of England rate of discount. (3) These deposits should be distinguished from specific deposits of wealth in particular forms which some customers usually entrust to their bankers for purposes of greater safety. The banker undertakes to return them, whenever wanted, in the exact form and shape they were entrusted to him, and not content himself by offering merely an equivalent. As the banker cannot easily use these deposits in his own business, and can have, therefore, no hope of making some profit for himself out of these he asks for some fee for taking charge of his customers' valuables.

The business world has realised gradually the value of banker's deposits ; and with the progress of education with the growth of business, the volume of deposits in every country has been growing. The following table showing the growth of deposits in the leading countries of the world in the last half-century is very instructive in this respect.

# Table showing the growth of Bank Deposits in some of the leading countries.

Foreign currencies converted into pounds sterling at approximately pre-war rates.

(In million sterling)

	1890	1895	1900	1905	1910	1915
England and Wales (excluding Bank of England) ...	368.7	455.6	586.7	627.6	720.7	992.6
France* ...	78.5	100.6	125.9	180.8	222.4	253.8
Germany† ...	42.9	53.2	86.1	151.2	226.4	435.3
India‡ ...	19.2	21.4	22.8	36.3	58.2	61.9§

\* Only Four leading Banks.

‡ For banks with capital of Rs. 5 lakhs or over.

† Only Six leading Banks.

§ For 1914.

Having collected his deposits the next thing for the banker is to seek the most profitable investment for the same. In employing the funds at his command the ordinary commercial banker must remember that by far the larger portion of the deposits are at call or short notice. He must, therefore, be always ready to meet any reasonable demand upon him. In normal times when the generality of the clients carry on their usual business with full faith in their banker's solvency, the temptation to the latter is very great for turning to account every available penny. The mark, therefore, which distinguishes a sound banker from an indifferent speculator in normal times, is the judgment with which each determines the amount of money he must hold against possible demands. No one—not even a banker of experience—can lay down a hard and fast rule as to the exact proportion of the total demand liabilities which should be held in cash or in easily, immediately realisable securities; for a great deal depends upon the general characteristics of the clientèle and the readiness with which the demand from one class of clients can be at any moment set off by the inflow from another class. The more varied the composition of the clientèle, the better their needs are studied, the safer is a business. The only principle that can, therefore, be safely laid down by us in this connection is that a banker must always hold a sufficient amount in reserve to meet all possible demands in ordinary circumstances.

With regard to sums which have been deposited with him for fixed and longer periods, and as regards the monies he creates by means of his own credit devices, the banker has a relatively free hand. But even here, a prudent commercial banker will not allow his zeal for profits to overcome his prudence in management. The banker must, therefore, so invest his funds as to be able always to realise them at the shortest notice with the least loss. To this end the best investment apparently is Government bonds—or “gilt-edged securities” as they are called. But unfortunately, as a rule these securities yield a very low rate of interest, and, in the event of any international complication, are liable to serious fluctuations. The tendency in the banking world is, therefore, not much in favour of large holdings in these securities. The most approved policy in this connection seems to be to invest in these securities sums not exceeding very much the total capital and the Reserve Fund. As regards the more profitable investment in industrial enterprise, the prudent commercial banker finds the constant fluctuations in the value of these securities, and the impossibility of realising them without a loss in the event of a scare or a crisis a sufficient bar to his temptations. He, therefore, turns more and more to the short term commercial loans, chiefly in the shape of discount of commercial paper. These are adequately secured by the legal liabilities of every party to each such instrument, and in case of an emergency are rapidly convertible without any appreciable loss. Though



the average rate of discount is, in well organised countries, usually not very high, the possibility of rapid turnover leaves the banker a sufficient margin of profit, after giving him all the security he can desire. Besides, at the same rate of interest the discounting business yields a greater net return. In all such instruments the chief and primary security is the personal liability of the parties to the bill; but the banker is not excluded from getting, if he so desires, some additional, collateral security in the shape of the goods against which these bills are drawn. Collateral security becomes important when advances are made by a banker for accommodating a customer, and in this branch it is necessary for bankers to know the financial standing of the customer as well as the value of his business, or any other security offered.

The foregoing remarks apply chiefly to banking business in normal times. For provision against abnormal times the banker must redouble his prudence and caution. If he is to pass safely through all crises, he must never engage in any speculative business himself, and discourage as much as it lies in his power the speculative tendencies among his customers, by taking double the ordinary precautions in financing clients, who, to his knowledge, are engaged in no sound business at all. Some sort of speculation in taking risks—is incidental in every business and inevitable even for the best businessman. The banker, therefore, cannot make a rigid rule for his guidance never

to finance any speculator at all; but we do not think it is too much to expect from sound and prudent bankers that they should be able to differentiate between the inevitable, ordinary risks of a legitimate business, and speculation pure and simple. Moreover, as a further pledge against panics, we might require that the banker should keep his resources as far as possible liquid or easily realisable. This, of course, is a matter essentially of individual discretion; and the practice of no two bankers would be exactly alike in all particulars. But, if the practice of the oldest or the best established banks is any indication for a course of conduct, the following table showing the average balance sheet of English banks would have its own value.

The English banks, we see from this table, are holding. p. c. of their total liabilities in cash. This is not universally commended, and may not be acceptable in all countries alike. Their holdings of consols was diminishing even before the War thanks to the fall in the value of these securities. Commercial paper, and short loans thus form the bulk of their investments, and they have found in it sufficient of security and high enough profit to induce them to go on with the same in ever increasing proportions.

## II. FINANCING TRADE.

We have already discussed this function incidentally while we were dealing with the prime function of the banks in collecting and utilising the

# Comparative Statement of Joint-Stock Banks of England and Wales ( Excluding Bank of England ).

[ In thousand pounds. ]

Year.	Bank.	No. of Branches.	Capital and Reserves.	% of Liab- ilities.	Deposits.	% of Liab- ilities.	Acceptances.	% of Liab- ilities.	Total Liabilities.	Cash in Hand and Money at Call & Notice	% of Liab- ilities.	Investments.	% of Liab- ilities.	Discounts and Advances	% of Liab- ilities.
			£	£	£	£	£	£	£	£	£	£	£	£	£
1880	104	2,203	67,826	14.5	368,663	79.4	22,693	4.9	464,075	83,955	18.0	82,816	17.8	269,507	58.0
1895	99	2,690	69,213	12.4	455,561	81.6	23,724	4.2	558,744	111,208	19.9	107,498	19.2	311,678	56.7
1900	77	3,757	78,847	11.3	586,726	84.0	21,550	3.0	698,762	144,400	20.7	127,766	18.3	895,313	56.6
1905	59	4,558	82,010	10.8	627,529	82.6	39,225	5.2	758,712	179,530	23.6	131,731	17.3	401,485	52.9
1910	45	5,202	80,946	9.4	720,687	83.6	52,263	6.0	862,134	199,724	23.0	137,711	16.0	467,880	54.3
1915	37	6,027	81,731	7.1	992,555	86.4	62,512	5.5	1,146,807	262,453	22.9	310,771	27.0	508,617	43.9
1916	35	5,993	81,089	6.2	1,154,877	87.9	68,726	5.2	1,316,220	369,460	28.0	323,002	24.6	542,773	41.4

another, and the possible development of trade in the near future between them. These requirements demand some amount of specialisation, and as all banks are not equally inclined to, or competent for, this sort of business, those which undertake it are now coming to be known as Exchange-Banks.

In the absence of the facilities which the Exchange-Banks give to the development of international trade, all the international dealings would have to be settled by being paid for in gold—the money-material most easily transportable, and universally acceptable. If the English wine-merchant buys £ 1000 worth of wine from France, and the French woollen dealer buys £ 1000 worth of woollen stuff from England each of this would have to pay £ 1000 in gold, and there would therefore be a double stream of gold to and from England. The Exchange banker, however, tries to avoid the cost of this double transport of gold—something like 1 d. per £ each way or about £ 4 in all—by setting off these transactions against one another and paying only the balance, if any at all. The Exchange banker, therefore, renders an important service by economising the use of gold, and incidentally, encouraging trade, since the number of transactions—and, therefore, the total trade—would have been very effectively limited, if each transaction could only be settled by a direct payment in gold. The profit of the Exchange banker is derived from the fluctuations in the value of the currencies of the different countries.



Without going into all the intricacies of the mechanism of Foreign Exchanges, it may be said that even with regard to countries that have the same standard of currency, the respective values of their local currency in terms of other currencies vary according to the state of trade between the two countries. If the total indebtedness of all French merchants to English merchants, exceeds that of the latter to the former, some gold will have to be shipped from France to England to liquidate the balance; and though the English pound sterling and the French franc remain of the same weight and fineness, the value of the French franc in terms of the English sovereign will fall to the extent of the cost of transport and insurance; or, what is the same thing, the French merchants would have to pay their debts plus the cost of sending gold to England. As the state of trade between England and France varies from month to month or week to week, the value of the two currencies frequently changes; and the banker makes a profit out of these changes, as much as by preventing the cost of transporting gold. The variation is of course much greater between countries which have two different metals for currency; but it does not follow therefrom that the banker's profits would be proportionately greater from the exchange business between such countries. There is in this business an element of speculation which makes the average gains much smaller and the business itself less commendable.

### III. SERVING AS GOVERNMENT

#### FINANCIAL AGENTS.

Though banking is originated from the requirements of private commerce, its connection with the Government in every country becomes more intimate every day. Modern governments are most interested in all the factors that effect the financial world. Nearly all of them have to borrow large sums to finance their public enterprise, or to prepare for any untoward political contingency. A good many of them have a system of currency which could not be managed without the aid of expert banking advice. Even in their ordinary transactions the receipt of their revenues and paying of their expenses would become much easier if the services of a Bank were at the disposal of the Government. Hence we find in most countries in Europe a bank more or less connected with and under the influence of the State, and entrusted with the receipt of Government dues and payment of public expenses, the management of national debt, and of the country's currency, and the floating of large loans for the purposes of the state. The importance of these functions to the general business community in a country depends very much upon the degree of centralisation. But as this would involve a comparative sketch of the organisation of banking in the leading countries, we think it beyond the scope of this work and as such we omit it.

## IV. THE ISSUE OF CURRENCY NOTES.

In the history of banks this last function has at one time been the most important. With the exception of the United States and Canada, where many banks are still allowed to issue notes, this function tends to become more and more centralised. We have already considered at length the principles that should guide the issue of notes through the agency of banks in a previous chapter, and we see no need, therefore, to enlarge upon it in this connection.

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## CHAPTER II.

### **Organisation of Banks in India.**

"The Money-market and Banking system of India comprise the following as its main constituents:—The Presidency Banks, European Exchange Banks the Indian Joint-stock Banks and the Shroffs; Marwaris and other private bankers and money-lenders." \*

At the head of the banking enterprise in India are the three Presidency Banks which are not only the oldest but the most powerful among the banking establishments in India. The Bank of Bengal led the way in 1806, with a capital of Rs. 50 lakhs, of which 20% was contributed by the East India Company. However it must be noted that the earliest banking house, on a European model, was started in India as early as 1770 and was styled the Bank of Hindostan, which did business long after the Presidency Bank of Bengal was established. The Bank of Bombay followed more than a generation later (1840) with a capital of Rs. 52,25,000 of which Rs. 3,00,000 was subscribed by the Government. By 1864 its capital was raised to Rs. 2,09,00,000, but it suffered so heavily during the collapse of the share mania in Bombay in the

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\* J. M. Keynes: Indian Currency and Finance.



sixties that it had to be reconstituted and registered as a Joint Stock Company with a capital of Rs. 10000000 under the title of the New Bank of Bombay, its title being again changed in 1876, when the Presidency Banks' Act came into force. The Bank of Madras which was started originally with a capital of Rs. 30 lakhs, of which Rs. 3 lakhs were subscribed on behalf of the East India Company, has had a continuous history of now nearly three quarters of a century (1843-1917); and, though compared to the gigantic strides made by its two sister institutions it has had an uneventful history, the Bank of Madras, too, has a remarkable tale of prosperity to tell.

From their origin these Banks had a close connection with the Government of the Company, which not only subscribed part of the capital, but also had a right to nominate some of their Directors. The office, moreover, of the Secretary and Treasurer of these Presidency Banks was held upto the time of the Mutiny by a covenanted Civil Servant of the Company. In return for such control exercised over them by the Government the Banks obtained some valuable concessions from the former. Chief among these concessions was the right of note-issue, at that time considered to be the most important of the functions and privileges of a banking institution. This right, however, it must be mentioned, was of little practical utility either to the Banks themselves or to the public, owing to several restrictions imposed by their charters.

Their total liabilities on demand, for instance, were not to exceed three times their cash reserves at first, and four times afterwards; from 1839-1862 even the total amount upto which the notes could be issued by these Banks was fixed by law. In 1862, following the Paper Currency Act of the preceding year, this right was taken away; but to compensate the Presidency Banks for the loss of this valued privilege it was decided to keep the whole of the Government cash balances at the Presidency Towns with these Banks. The value of this compensation almost disappeared in 1876, when, owing to difficulties which had arisen with regard to the withdrawal of Government moneys from the Bank of Bengal in 1863 and from the Bank of Bombay in 1874, the Reserve Treasuries were created and the cash balances of Government with the Banks were greatly reduced. It was decided in this year to effect the most drastic changes in the relations of the Presidency Banks with the Government. Government also sold their shares in the Presidency Banks, and abandoned their right of being represented on the Directorial Boards of these institutions.

The Presidency Banks in India, therefore, are in no sense of the term State Banks. They are private institutions formed by private enterprise, and conducted by private individuals. The bulk of their business is that of any ordinary bank, but we cannot say even now that they have no connection with the State. Government are entitled to audit

their accounts if they think it necessary, to call for any information regarding the business of the Banks, and to ask for the production of any document relating to their affairs. They are also required to publish such statements of their assets and liabilities, at such intervals and in such form and manner as Government may think fit. These various methods of public control, however, indicate rather a desire on the part of the Government to instil a salutary fear of public watchfulness on the affairs of the institutions, which, from their standing as well as their traditions, may conceivably be taken by other institutions of their kind as models, and thereby set the tone to the whole banking enterprise of the country, than as showing any intimate connection or dependence of the Banks upon the Government. The Presidency Banks, it is true, are allowed the custody of a certain amount of public balances ; but this amount is just enough to compensate the Banks for conducting the work of the Government Treasuries. The Government are not bound by any undertaking to keep a balance either at the head offices or at any of the branches of these banks ; but there is an undertaking that in the event of the balance at the head office of each bank falling below a certain stated figure, varying in the case of each Bank, Government will pay interest on the deficit.

The same tendency of exercising a minute control over the business of the Banks, without, how-

ever, having any financial interest in their development, is observable in the restrictions which were copied by the Presidency Banks Charter Act of 1876 and which have succeeded in preventing their rapid development. Chief among these restrictions are:—

(1) the drawing, discounting, buying and selling of bills of exchange and other negotiable securities is confined to bills and securities payable in India except in the case of the Bank of Madras which is allowed to do business also in bills and securities payable in Ceylon.

(2). Borrowing of money is allowed in India only.

(3). Loans or advances upon mortgage or in any other manner upon the the security of immovable property or the documents of title relating thereto are expressly prohibited.

(4). The amounts which may be advanced to any individual or partnership firm by way of discount or on personal security is limited to an amount prescribed in the bye-laws of the Bank, such bye-laws having been previously approved by Government.

(5). Loans or advances cannot be granted for a longer period than six months.

(6). Discounts cannot be made or advances on personal security given, unless such discounts or advances carry with them the several responsibilities



of at least two persons or firms unconnected with each other in general partnership.

If we examine these restrictions carefully we cannot but perceive in them the spirit of jealousy of which the East India Company, all through its existence, could not altogether rid itself. The Company had their own vast banking transactions; they feared too great a growth of the Presidency Banks as a likely source of their own weakness; they, therefore, imposed such restrictions as would effectually prevent the Banks from ever becoming serious rivals of the Company. Apart from this dread of a formidable rival, the Government of the Company must be credited, in fairness, with a genuine desire that semi-public institutions like the Presidency Banks will lose nothing if they are conducted on the safest possible principles in a country like India where the paramount power had, in the first half of the last century, yet to establish its credit, and where banking on European lines was yet a novelty. Moreover in 1876 when these provisions were reshaped, the Government were just witnessing rapid and violent fluctuations in the exchange value of the rupee. The first two restrictions were, therefore, imposed to preclude the Presidency Banks from a possibly profitable but a certainly perilous kind of business.

At the present moment, however, these restrictions are bound to operate with undue harshness upon the Presidency Banks. Government no longer keep with them such large amounts that, in the

interests of the general public, the Government may be held bound to place such restrictions on the general banking business of these institutions. Besides, the exchange value of the rupee is no longer subject to any great fluctuations. And the Presidency Banks, by dint of careful management, have reached a stature, which, without any assistance from the state such as the great State Banks of Europe obtain as a matter of right from their respective governments, and without any of the privileges which make the private Bank of England the predominant institution in the country, has made them the ultimate resort of the Indian money-market. They may reasonably claim, therefore, that these antiquated provisions which unnecessarily restrict their development should be removed, and that they should have some means open to them of increasing their resources in India in times of pressure. The best means of giving them these facilities is to allow them to borrow in London. The Government of India, it may be noted, were willing to meet the wishes of the Banks in this respect; but in 1906 the Secretary of State finally negatived the proposals, and there the matter rests for the present.

In this sketch of the working of these Banks we must not omit to mention the common allegation that the need of the commercial public and the ingenuity of the Bank officials have combined to defeat the spirit if not the letter of these provisions. Under a provision which prohibits them

from lending on promissory notes bearing less than two independent signatures, they have, paradoxical as it may seem, found means to evade some of the other restrictions. The letter of the Presidency Banks' Act will be satisfied if any two names are obtained, but as any two names may not necessarily, be good security, the Bank may then, for prudence sake, accept some other collateral security which is forbidden by the letter of the law. But in reality there is no evasion of the Act in this. The Banks are not prohibited from taking any collateral security if they consider the value of the original security has deteriorated. If, for example, it has come to their knowledge that one of the obligants has lost heavily in speculation, they would be right and entitled to call for further security of any kind to secure their debt. This additional security is, however, never taken in the first instance, and so there is no evasion of the Act. The Banks also evade, it is said, the provision that they should not lend upon goods, or title to them, unless they are deposited with them, by establishing a kind of bonded warehouse of their own; and when the goods in question are too bulky to be removed to the Bank's own warehouse, the same purpose may be served by the borrower's shop, or Mill, or warehouse or other place of business by the expedient of taking the watchman on these premises into the pay of the Bank. Here also the Bank might plead there is no evasion; since the Act does not say where the goods may be stored. And so

long as they are in a building rented by the Bank under their lock and key the provisions of the Act are in no way evaded. The provision, again, which forbids them from making advances for a longer period than 6 months, can be evaded by the simple expedient of renewing such loans at the expiration of the statutory period of six months. All these would illustrate the remark that it is futile to try and regulate the concerns of such a daily growing institution as a Presidency Bank by an Act of Legislature forty two years old.

The business of these Banks at present consists of:—

(1). Investment of money in any securities of the Government of India, or of the United Kingdom, the stock or debentures of, or, shares in Railways bearing a Government guarantee in respect of interest, and the debentures and securities of any Municipal body or Port Trust in India, or of the Bombay Improvement Trust; also the alteration, conversion and transposition of these investments.

(2). Advancing money against any of the securities specified above or against bullion or other goods which, or the documents of titles to which, are deposited with, or assigned to the Banks as security.

(3). Advancing money against accepted Bills of Exchange and Promissory Notes.



(4). Drawing, discounting, buying or selling of Bills of Exchange and other negotiable securities payable in India or Ceylon.

(5). Receiving deposits.

(6). Receiving securities for safe custody and realisation of interest etc. from the constituents of the Banks.

(7). Buying and selling of gold and silver, whether coined or uncoined.

(8). Transacting pecuniary agency business on commission.

(9). Management and conduct of Government loans in Presidency towns.

(10). The management of debt of certain Municipalities, Port Trusts, and Improvement Trusts throughout India.

Most of these functions are the ordinary functions of commercial Banks, and they are all noteworthy because of the implicit or explicit restrictions placed by law upon them. It may be noticed, however, that the permission to buy gold and silver, coin or bullion, is interesting not only because it has greater affinity with the business of money changing than with banking business proper, but because it has the occasion of the failure of the Indian Specie Bank in 1913. If the Presidency

Banks could be permitted to engage in such business, the other banks thought it not at all risky to follow suit. Money changing or bullion dealing was, however, transformed by them into silver speculations with the melancholy results with which we are all familiar. The Presidency Banks, we may notice, were allowed to manage the Government Savings Banks, upto 1896-97, when they were transferred to the Post Office.

The Presidency Banks have of late shown a commendable zeal in widening the scope of their activity even within the restrictions of their statute. They are opening new branches, and the Bank of Bombay has within the last year opened two branches in two busy localities of Bombay. On the working of these branches it would perhaps be premature to pronounce any opinion just now; but the remark may be ventured that the multiplication of such branches is one of the greatest needs of banking business in India. Without a wider branchification our Banks will never be able to tap the savings of the small investor; and unless they do so the industrial development of India must be postponed for a long time.\* (2) The Presidency Banks, more-

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\* On December 31st 1916 the Presidency Banks had branches as follows:—

Bank of Bengal	..	..	22
„ Bombay	..	..	16
„ Madras	..	..	24

over, have offered to co-operate with the Government in their desire to encourage the more extensive use of currency notes. They have undertaken to issue and exchange for cash on behalf of the Government Universal Currency Notes freely at all their branches. In return Government have agreed to maintain certain minimum balances at such branches so long as they are entrusted with this work. It is generally known now that in regard to their balances, Government intend to follow a more liberal policy in relation to the Presidency Banks in pursuance of the recommendations of the Chamberlain Commission. We have referred to this subject of the cash balances of the Government of India in another chapter. Let us repeat here that during the busy season, when trade is active and the demand for money, is great, Government locks up considerable sums in public treasuries, for the season of busiest trade is also the season of the heaviest collection of public revenues. The figures of the closing balances on 31st March 1913, were:—

In 270 District Treasuries	£ 6,590,500
„ 35 Branches of Presidency Banks	2,198,300
„ 3 Head Offices „ „	1,595,600
„ 3 Reserve Treasuries	8,908,700
	<hr/>
	£ 19,293,100

It is said the normal balance required by the Government of India is £ 12 million or Rs. 18 crores ; so that on the above date £ 7 million or nearly Rs. 11 crores, was locked up in the Reserve Treasuries just at the moment when the business world needed most assistance. The Chamberlain Commission observe. "It appears to us that a system which leads in certain circumstances to the locking up of nearly £ 9,000,000 during the busiest period of the commercial year, and £ 5,400,000 more than under the same system was similarly locked up in the previous year, requires very strong justification..... We have said that Government cannot sacrifice the interests of the general tax-payer to the interests of the trade. Nevertheless we should be the first to recognise the immense importance of trade to the prosperity of the country and the revenues of Government. The principles now observed result in loans being granted from Government balances only in exceptional circumstances, and while there is a provision that Presidency Banks may retain, on payment of interest, sums in excess of those which it is the practice to leave with them, this provision has had little publicity and has not been acted upon". Accordingly the Commission proceeded to make two alternative recommendations : (1). the closing of the Reserve Treasuries, and placing of the whole of the balances of Government at Calcutta, Bombay, and Madras with the head office of the Presidency Banks; or (2) in the alternative, the making of loans directly by the Government from their



balances. In the former case, though owing to the great expansion of the business of the Presidency Banks, the proportion of the increased public deposits would be very small compared to the other deposits, the amount under this recommendation would still be considerable, and it is pointed out that it would be injudicious to encourage the rather restricted money-market in India to rely too much on Government funds. The bulk of opinion in the Commission seemed to support the second alternative; and, it must be admitted, in the absence of a State Bank, it seems to be more reasonable.

Further expansion of the business of the Presidency Banks could be suggested in various directions, as for instance, opening an industrial branch. The advisability of such a measure however, we shall discuss in a later and more appropriate chapter. Another means of developing their business would be a redistribution of territory. Under the present arrangements each of these Banks is assigned a definitely marked territory, which is the largest in the case of the Bank of Bengal, and very limited in the case of the other two Banks. These latter believe—and quite reasonably,—that if there was a redistribution of territory now their business would grow very much. Let us here conclude this short sketch of the working of the Presidency Banks, by giving a table, showing their development and present position.

Table showing the progress made by the three Presidency Banks from 1870 to 1916.

In lakhs of Rupees.

31st Dec.	Capital.	Reserve and Rest.	TOTAL.	DEPOSITS.		TOTAL.	CASH BALANCES
				Government Deposits.	Other Private Deposits.		
1870	336	226	362	543	640	1183	997
1880	350	555	405	291	849	1140	741
1890	350	998	448	359	1476	1836	1297
1900	360	200	560	281	1288	1569	504
1905	360	263	623	312	2226	2538	823
1906	360	280	640	308	2745	3053	1095
1907	360	295	655	336	2811	3147	948
1908	360	309	669	326	2862	3188	1039
1909	360	318	678	320	3265	3585	1166
1910	360	331	691	424	3234	3658	1135
1911	360	340	700	438	3419	3858	1358
1912	375	364	739	427	3584	4011	1177
1913	375	373	748	589	3648	4237	1538
1914	375	389	764	562	4004	4565	2084
1915	375	331*	706	487	3860	4347	1464
1916	375	307*	682	521	4471	4996	1726

\* Excluding reserve for depreciation of Investments.

## **The Exchange Banks.**

Since the Presidency Banks were forbidden to deal in foreign exchanges, or to raise money outside India, a very important field for banking in India was left entirely uncultivated by them. The business of financing the foreign trade of India was bound to grow as the volume of that trade increased; and as the Presidency Banks could not enter that field, another class of Banks had to be developed to meet this growing need. The Exchange Banks were, therefore, started with the intention at first of confining their operations to the foreign exchanges in India; but they have since so widely extended their functions that they now transact every kind of banking business permissible to banks in India. The official definition of an Exchange Bank requires that the head-office of such a bank should be outside India; but for convenience' sake we may take all those banks to be Exchange Banks which deal principally in the two classes of business from which the Presidency Banks have been excluded. This distinction is more convenient as the new Indian Joint Stock Banks, though they have proved serious rivals of the Exchange Banks in India, do not engage to any considerable extent in financing the foreign trade of India, nor have they, as a rule, any branches outside India. The Indian Specie Bank, during recent years was the only Bank of Indian origin, which had a branch office in London; but the branch was meant more to facilitate the dealings in silver

and pearls than with any intention to take up any portion of the usual business of the Exchange Banks.

Even the Exchange Banks proper may be divided into two groups according as their principal business is with India or is only a small fraction of their total business in India. The opening up of India to every enterprising nationality, and the consequent settlement for commercial reasons of various European, American and Japanese merchants in India has led to branches of some of the principal Banks in those countries being opened in India. Thus France has a branch of the Comptoir National d'Escompt de Paris, Russia of the Russo-Asiatic Bank, Japan of the Yokohama Specie Bank, and also that of the Sumitomo Bank, America of the International Banking Corporation in India to finance—we may presume—the trade of their countries at least with India. Before the war there was also a branch of the Deutsche-Asiatische Bank in India to help in the no inconsiderable trade of Germany with India. Such banks are a great asset to those countries. We have no means of determining what proportion of their total business is transacted in India ; but as each of these is a well-known banking establishment in its own country, and consequently with wide business connections throughout the world, we may be sure their Indian business, however valuable in itself, is very little on the whole.

Most of the remaining Exchange Banks have their principal business in India. They are:—



The Delhi and London Bank founded in 1844 and now taken up by the Alliance Bank of Simla, the Chartered Bank of India, Australia and China founded in 1853, the National Bank of India Ltd. started in 1863, the Hongkong and Shanghai Banking Corporation founded in 1867, the Mercantile Bank of India, founded, under its present style, in 1893, and the Eastern Bank founded in 1910. Between 1864 and 1910 no new Exchange Bank was started which survives upto now, in spite of the fact that the business of these banks must be exceedingly paying if we are to judge from the quotations of their shares and the dividends they have been paying. The only explanation seems to be that the class of business these banks deal in is so entirely due to long and established connections that there is hardly room for the enterprising genius of an audacious outsider unsupported by the credit and connection of a well-known business house in India. However it can not be denied that if some leading firms like the Tatas and the Currimbhoys join hands it will not be difficult to start an exchange bank.

The business of these banks in India was originally carried on almost exclusively by funds borrowed outside India—chiefly in London—by offering much higher rates of interest than the English banks could give. Of late, however they have discovered that it is possible to attract deposits in India on almost quite as favourable terms as can be done in London, and a considerable proportion of the financing of Indian trade is now done

by these banks by funds raised in India. On December 31st, 1914, the Exchange Banks held Indian deposits amounting to over 30 crores of rupees out of the total private deposits with all Joint Stock Banks amounting to roughly  $88\frac{1}{2}$  crores of rupees. As a rule before the war, on fixed deposits received for a year or longer periods these banks allowed interest at  $3\frac{1}{2}$  or 4 p. c. or about 1 or  $1\frac{1}{2}$  per cent more than was allowed by the large Joint Stock Banks on similar deposits in London. On deposits received for shorter periods the rate of interest allowed varied; and on current accounts they allow 2 per cent in the slack and  $2\frac{1}{2}$  per cent in the busy season with some such conditions as the maintenance of a definite minimum monthly balance. It may be noticed in passing that the principal Banks in London do not allow any interest on current accounts, while the Bank of England does not allow interest even on fixed deposits.

Besides the usual banking operations of holding cash, money at call, and some investments, the Banks deal principally in the purchase and discount of bills of exchange. A part of these bills are negotiated in London and payable in India; but by far the larger portion consists of bills negotiated in India and payable in London. As the bulk of the export trade of India is very great, and as almost the whole of it is financed by these banks, they are often discounting quantities of bills which they can have no chance of holding until maturity; but the Banks get over this difficulty by a system of rediscount in

London. As a rule the bills against Indian exports are drawn at three months' sight and are either "clean," or "documentary"-accompanied by documents relating to goods against which they are drawn. They are drawn on well-known firms or against credits opened by banks or financing houses in England; and as, in addition to all these, they bear an endorsement of an Exchange Bank it is easy to rediscount them in London if required. Bills purchased in India are sent home by these banks by the first available mail; and if they are rediscounted immediately on their arrival in England the Exchange banks would, in normal times, have held these bills only for 16 or 17 days instead of the three months when they would be paid. Of course they do not rediscount all the bills purchased. If there is an expectation of a fall in England of the rate of discount; or if the parties responsible on a Bill are excellent and the Banks are not in immediate need of funds they may hold the bills for a longer period or even upto maturity. We may have some idea of the amount of bills these banks rediscount in London from the following figures:—

**Liability on Bills of exchange rediscounted and still current.**

Chartered Bank of India	£ 2,923,000
Eastern Bank	£ 565,000
Mercantile Bank of India	£ 2,202,000
National Bank of India	£ 3,387,000

The above figures, it must be noticed, do not relate to rediscounts of Indian bills alone, as the Banks operate in other parts of the world also; but as these banks have the bulk of their business in India, it may safely be assumed that Indian bills form a very large proportion of these figures.

The purchase of export bills in India is managed by the Banks in a variety of ways. Proceeds of the import bills as they mature are among the first of these methods. Sale of drafts, or transfers for Indian students or travellers in England, is another of these methods, growing in importance every year. But the most important of these is the purchase of Council Bills and Telegraphic Transfers payable in India. And when all these methods do not suffice to meet the needs of a brisk export trade, the Banks in the last instance import bars of gold or silver bullion, or sovereigns from London, Egypt or Australia.

This short sketch of the operations of the Exchange Banks in India may now be illustrated by the following table.



**Table showing the Capital, Reserve, Deposits, and Cash Balances of the Exchange Banks on 31st December each year.**

(In thousands.)

Number of Bank.	Capital and Reserve.			Deposits.		Cash Balances		Percent- age of cash to deposits in India.
	Capital.	Reserve and Rest.	Total.	Out of India.	In India.	Out of India.	In India.	
1870	2,004	180	2,184	£ 2,688	£ 349	£ 2,611	£ 408	116.9
1880	2,532	541	3,073	7,305	2,266	2,046	1,201	53
1890	6,384	1,699	8,083	30,734	5,024	5,810	2,336	46.5
1900	11,803	3,971	15,774	54,263	7,002	11,945	1,597	22.8
1905	15,204	7,219	22,423	94,536	11,363	21,504	2,521	22.2
1906	15,866	8,421	24,287	104,457	12,058	18,436	3,604	29.8
1907	16,671	9,320	25,991	94,78	12,773	14,860	3,735	29.2
1908	16,692	9,149	25,841	103,289	13,010	16,665	2,524	19.4
1909	18,952	11,211	30,163	116,024	13,516	18,121	2,772	20.5
1910	21,734	12,610	34,344	134,166	16,528	17,810	2,923	17.9
1911	22,600	13,001	35,601	157,764	18,779	22,136	3,046	16.2
1912	23,657	13,980	37,637	172,028	19,691	23,082	4,099	20.8
1913	23,640	14,185	37,825	181,138	20,690	25,688	3,922	18.9
1914	22,815	14,157	36,972	164,970	20,098	40,694	5,596	27.8†

\* Excluding the Deutsch-Asiatische Bank for which statistics are not available.

† This was probably due to the greater precaution necessitated by the bank failures of 1913-14.

From this table it appears that there is a certain amount of danger to be apprehended to the Banking system of India from the practice of the Exchange Banks of inviting considerable deposits in India without keeping an adequate cash reserve. The bulk of their funds is locked up in Bills, while the absence of any distinction in their published balance sheets between fixed and current deposits leaves us without any guide to estimate with accuracy the financial position of these institutions. Moreover they attract large deposits outside India; and these are usually for short periods. The entire financial system of India may have to suffer because our money market is financed by funds raised not permanently but for short periods. It is true, of course, that these banks are engaged in an exceedingly lucrative and comparatively safe business; but the general maxims of banking management and the requirements of banking prudence should not be lost sight of even by the best established houses.

### **The Indian Joint-Stock Banks.**

The Presidency Banks being taken up with business of a semi-public character, and having branches only in the large towns, and the Exchange Banks being fully occupied with financing the foreign trade of India, the great mass of the internal commerce of India was left without the aid of organised banking on the modern system. There were good reasons why the leaders of the European money-market in India should hold themselves aloof from the business of financing the local trade of India. That business, with all its intricacies of local usage

and variety of indigenous negotiable instruments, was, in the first place, unknown to them. They had, moreover, a very lucrative and safe business of their own to attend to. Even if the far-sightedness of some of them made them perceive the immense possibilities of that business, their prudence would not allow them to venture in an unknown, if profitable, enterprise. It was, therefore, left to the Indian entrepreneur to exploit the local commerce of India for its banking possibilities. The rise of the Indian Joint Stock Banks is of quite recent origin, though banking houses of the older type were known in India from time immemorial. The earliest bank of this description was the Bank of Upper India founded in 1863 and the Allahabad Bank followed in 1865. These are banks registered in India, with their head offices in India; but most of them are under European management. We can, therefore, hardly class them as exclusively Indian banks of the type of the Indian Specie Bank. The Alliance Bank of Simla was, at its foundation in 1874, of this class; but since its recent amalgamation with the Delhi and London Bank, it may more fittingly be classed as an Exchange Bank, than as an Indian Joint Stock Bank. The Oudh Commercial Bank founded in 1881; the Punjab Banking Company, founded in 1889 now absorbed by the Alliance Bank of Simla; and the Punjab National Bank founded in 1894 are all establishments conforming to the type of the Allahabad Bank except that the first and the third are entirely under Indian management while the others are almost wholly controlled by European. During the

next ten years no great Banks of this type were established; but with the outburst of Swadeshism in 1904 an entirely new type of Bank became important. The Bank of Burma was the first in the field, while two years later three other banks were founded viz. the Bank of India, the Bank of Rangoon, and the Indian Specie Bank. Since that date many other banks—financed by Indian capital and managed by European or Indian Directors—have been started, and some of them are still in existence with varying degree of success.

The object of these banks is to attract Indian deposits and to finance at least the internal trade of India. They offer as much as  $4\frac{1}{2}$  or 5 per cent on fixed deposits, for twelve months while on current accounts their usual rate is 2 per cent. Compared to the Presidency Banks and the Exchange Banks these conditions are very favourable; but they would not, for that reason alone, be at variance with the ordinary maxims of banking business, if the funds so attracted were used for more lucrative business. We have no precise indication as to the kind of business these banks enter into; probably the business of each of these banks varies with its clientèle, its general environment, and the predilections of its founders and managers. But, if we are to judge from the revelations of the proceedings of some of these banks in liquidation, many of them either engaged themselves, or financed clients who were engaged, in speculative businesses of the worst descriptions. We give below a table which tells its own tale.



**Table showing the Capital, Reserve, Deposits, and Cash Balances of the Indian Joint Stock Banks, classified in groups according to the amount of Capital, on 31st December 1914.**

(In thousands of Rupees.)

	No. of Banks. 1	Paid-up Capital. 2	Reserve and Rest. 3	Deposits. 4	Cash Balances. 5	Percent- age of 5 to 4
Banks with Capital and Reserve amount- ing Rs. 20,00,000 and above ... ..	5	1,39,14	1,09,56	13,75,66	2,92,00	21·2
Banks with Capital and Reserve between Rs. 20,00,000 and Rs. 10,00,000 ... ..	9	92,38	27,11	2,72,14	54,18	19·8
Banks with Capital and Reserve between Rs. 10,00,000 and Rs. 5,00,000. ... ..	3	19,88	5,21	62,78	7,00	11·2
<b>Total of Banks above Rs. 5,00,000 ... ..</b>	<b>17</b>	<b>2,51,40</b>	<b>1,41,88</b>	<b>17,10,58</b>	<b>3,53,18</b>	<b>20·6</b>
Banks with Capital and Reserve between Rs. 5,00,030 and Rs. 1,00,000... ..	25	42,22	13,02	1,26,54	27,99	22·0
<b>TOTAL ... ..</b>	<b>42</b>	<b>2,93,62</b>	<b>1,54,90</b>	<b>18,37,12</b>	<b>3,81,17</b>	<b>20·7</b>

From the above table it is clear that the cash reserve of the 42 Joint Stock Banks was only a little 20 p. c. even at a time when almost all the weak banks had disappeared and the surviving ones had strengthened their reserves. We have not been able to get figures to find out the percentage of cash to deposits held by the Indian joint stock banks before the bank failures of 1913 and 1914 but it is quite clear that it must have very low. It was, perhaps, this more than any other single factor which explains the heavy bank failures of 1913. The way was led on the downward path by the Peoples' Bank of India on September 17, 1913, and since then 63 banking houses in all have failed. The figures alone of the authorised, subscribed, and paid up capital show how unsound was the foundation on which all these houses rested. The aggregate authorised capital of these 63 banks was Rs. 10,13,80,000 out of which only Rs. 4,12,58,000 or 40·7 per cent were subscribed and Rs. 1,46,15,000 or only 14·4 percent of the authorised capital and 35·4 per cent of the subscribed capital were paid up. The following table, giving the figures of capital, Reserve and deposits of the principal banks that went into liquidation between 1913-15, will show at a glance that the ultimate disaster would have seemed inevitable to any one who had been carefully watching the situation in the Indian money market between 1910-1913.

## In Lakhs of Rupees.

Name.	Paid up Capital.	Reserve.	Deposits.
Bank of Upper India (1914)...	10	9	154
Bombay Banking Co. ...	1	...	15
Credit Bank of India ...	10	...	51
Deccan Bank Limited ...	1	...	11
Hinduism Bank ...	1	...	11
Indian Specie Bank ...	75	15	270
Kathiawad and Ahmedabad Banking Corporation ...	7	...	23
Lahore Bank Limited (1914) ...	1	...	29
Marwar Bank ...	2	...	8
People's Bank of India.	13	2	126
Pioneer Bank ...	3.84	...	1.96
Punjab Co-operative Bank (1914)...	8	2	466
Popular Bank ...	3	...	19

If we examine carefully the causes of these failures, apart altogether from the culpable neglect of the very elementary principles of banking business, we cannot but admit that criminal mismanagement has also much to say in this series of disasters. In the times of growing prosperity, during which those banks had come into being, the neglect of ordinary banking prudence is at least intelligible if not pardonable. But the disclosures in public courts

attendant upon the first failures showing extravagance, dishonesty and criminal mismanagement to an unprecedented extent gave a shock to public confidence from which the new banks could hardly recover. Their position being unsound from the beginning, they were yet able to carry on their business so long as a gullible public believed in them as a new device for making the utmost money in the shortest time with the least trouble; but when that belief was shaken, it was but an easy stage from distrust to rush, and then to panic leading finally to collapse. The leading criminals were, it is true, at last punished; but the injury they did to banking business in India, in particular and to the industrial and commercial development of the country in general was-if not irreparable-so deep and lasting that many have thought indigenous banking institutions impossible in India in the near future.

Without, however, attempting in any way to palliate the gross mismanagement and breach of trust which some of the managers of the new banks were undoubtedly guilty of, we may mention that their criminal mismanagement is explained by their utter inexperience of the theory and practice of banking. The men at the head of these institutions were energetic and enthusiastic; but they were utterly unfit for the direction of a banking business. Perhaps they hoped for the best even in their maddest freaks; perhaps they sincerely believed that engaging in pearl or silver speculation by themselves,



or financing heavily clients who engaged in such operations was in the best interests of their constituents. In any case when new enterprises were started it was assumed that men who had been marked successes in other walks of life might as well direct a banking business; and because men with the necessary qualifications were entirely unavailable, these men, in spite of their ignorance and inexperience, were placed at the head of affairs. The earlier English Joint Stock Banks too suffered from similar causes. Gilbart in his book on Banking Vol. II says "Thirdly, and perhaps this was the greatest handicap of all, both directors and officials were often sadly lacking in practical experience of the management of a bank." In many of the early Joint Stock Banks none of the directors had had any acquaintance with banking methods previous to their appointment on the board of the company. Many of the officials were in a similar position; the supply of thoroughly trained men was entirely inadequate, and to get over the difficulty, recourse was had to men who enjoyed high social standing. He would have been a bold man who in 1910 would have prophesied troubles merely because the men at the head of the new banking institutions in India were lacking utterly in any theoretical knowledge of their subject, nor had they in any way made up for their deficiency by serving a practical apprenticeship. The value of special training is apt to be ignored in a new country with almost a virgin soil for human enterprise; but a total neglect of

special training for a long period is bound to bring a lesson, all the more lasting because it has been—it had to be—learnt at a heavy cost.

### III THE NATIVE BANKING HOUSES.

The last section of the Indian money-market consists of the shroffs or private bankers, who have been known in India from earliest times, and whose importance is even now not obscured by any of the modern banking institutions in India. In times gone by the principal business of the shroff was to change money, to give letters of credit from one place to another, and even, on occasions,\* to help the state in financing a great undertaking. The first two functions are evidenced not only by the records of all foreign travellers in India as well as by the universal tradition in the country itself, but also by their most prominent business even today. As regards the third we have evidence of the Nagarsheths of Bengal, for instance, being required to pay a heavy loan to the local Nawab in his wars against his neighbours. The loan, it is true, would only be a enphemism in the mouth of an unscrupulous autocrat; but as the shroffs—like the Nagarsheths of Bengal,—were the only people with considerable amounts of ready money which was always welcome to the ruler who had something more than the mere plunder of the country at heart, they were, comparatively speaking, immune from any arbitrary

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\* One Bansilal Abhechand gave great assistance to the Bengal Government during the Mutiny. (*Times of India* 27-9-1895.)

exercise of autocratic powers in violation of their rights of property. And even in the altered conditions of to-day the shroff continues to be the indispensable middleman of the Indian money-market. From their very nature the foreign banks in India can never hope to get into sufficiently close touch with the vast trading community of the whole of India; at most they can expect to finance the traders of the places where they have their branches or agencies. The shroff, therefore, acts, and must for a long time continue to act, as the banker for this large community. He buys their bills at a fairly high rate of discount for ready money; and if he is himself momentarily embarrassed for funds he need but go to the best banks in his city who will only be too pleased to rediscount bills with his signature. In this way he brings a volume of business to the Presidency Banks, which under the Presidency Banks Act, could not otherwise have been accepted by those Banks. As the shroff, for his own interest, keeps in close touch with the entire trading community, and as he, normally speaking, would not undertake liabilities beyond his ability, the Presidency Banks find this business of discounting bills with a shroff's endorsement a perfectly safe and an exceedingly remunerative one. For the shroff can afford to pay a stiff rate of discount—as the banks would call it—as he himself has charged perhaps a still higher rate. Naturally there is no uniform rate at which the shroffs discount the native Hundies. It varies very much according to the

standing of the borrower and also according to the prevailing bank rate for discount. Generally speaking however, a charge of  $1/8$  per cent per month above the bank rate of discount is the average rate charged by the Bombay Shroff to a first class borrower. In Calcutta and Madras these rates are a little higher owing to the absence of that keen competition which distinguishes the shroffs of Bombay.

The shroffs who engage in this occupation are principally Marwaris and Multanis with their head offices in Bikanir and Shikarpur respectively. Elsewhere their business is carried on by their Munims or managers who have very extensive powers. We do not know to what extent these native bankers receive deposits and engage in exchange business throughout India; but some estimate may be formed from the subjoined table. They lend money on mortgages, they do a regular commission business and then often speculate heavily in all kinds of produce. These figures, it must be noted, are so very different in the two years because since the outbreak of the war the Marwari shroffs, have generally speaking, discontinued their endorsing business.

Name.	Discounts current on June 30, 1913.	Discounts current on June 30, 1916.
Bank of Bengal	232 lacs	224 lacs.
„ „ Bombay	216 „	98 „
„ „ Madras	152 „	82 „



We may close this chapter by a brief account of the Bankers' Clearing Houses in India. The system of clearing houses was found indispensable in England towards the last quarter of the eighteenth century, and has since then aided considerably in the development of banking business by facilitating the rapid settlement of countless cross claims. Since almost each bank in a great business centre is sure to have every day credit and debit items with all the other banks in that centre it would save and simplify business if, instead of all those items being paid or received in cash, they were discharged against one another, only the balance, if any, having to be paid. It is this great advantage of a clearing house system which explains the phenomenal development of the cheque system in England. For the greater success of this system it is necessary that one of these banks should act as the settling Bank—or Bankers' Bank. If all other banks habitually keep a balance at one bank, they need not even pay the balance in hard cash, but only by an order or cheque on the Banker's Bank, which, being credited or debited in the accounts of that Bank, would finally settle the claims of all against one another, without a single pie passing from one bank to another.

The principal clearing houses in India are those of Calcutta, Bombay, Madras and Karachi, and of those the first two are by far the most important. The Presidency Banks, the Exchange Banks, English Banking agency firms, and the leading Indian Joint Stock Banks are members of these clearing houses.

No bank is entitled to claim membership as of right, while an application for admission must be proposed and seconded by two members, and be subject thereafter to ballot by the existing members. The Presidency Bank at each centre acts as the settling or Bankers' Bank; a representative of each member attends at the office of that Bank on each business day at a certain time to deliver all cheques he may have negotiated on other members and to receive in exchange all cheques drawn on his bank by the latter. After all the cheques have been received and delivered the representative of each bank advises the settling bank of the difference between his total receipts and deliveries, and thereupon the settling bank strikes a final balance to satisfy itself that the totals on either side tally. The banks with debit balance arrange to pay the settling bank the amount due by them during the course of the day, and the latter in turn arrange to pay on receipt of the amounts the balances due to the creditor banks. As all members have an account with the Presidency Bank the final balance is usually settled by cheques and book-entries.

The clearing house returns may be taken as some indication of the development of banking. In India, however, most of the local Joint-Stock Banks being excluded, these returns merely represent the transactions of members only, which is not quite reliable for estimating the total number of cheques cleared. The following table, however, is

given in the hope that it would throw some light on the development of banking in India.

Total amount of cheques cleared annually.

In Lakhs of Rupees.

Year.	Calcutta.	Bombay.	Madras.	Karachi	Total.
1901	Not available.	6,511	1,338	178	8,027
1902		7,013	1,295	268	8,576
1903		8,762	1,464	340	10,566
1904		9,492	1,536	365	11,393
1905		10,927	1,560	324	12,811
1906		10,912	1,583	400	12,895
1907	22,444	12,645	1,548	530	37,167
1908	21,281	12,585	1,754	643	36,263
1909	19,776	14,375	1,948	702	36,801
1910	22,238	16,652	2,117	755	41,762
1911	25,763	17,605	2,083	762	46,213
1912	28,831	20,831	1,152	1,159	52,835
1913	33,133	21,890	2,340	1,219	58,582
1914	28,031	17,696	2,127	1,315	49,169
1915	32,266	16,462	1,887	1,352	51,967

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## CHAPTER III.

### **Peculiarities of Banking in India and some suggestions.**

We have now completed a brief sketch of the organisation of the money-market in India and a critical examination. Several points in this sketch seem to need further elaboration and explanation.

(1) At first glance the student would be apt to imagine that there was a well-defined, distinct field of business for the activity of each kind of bank. The Presidency Banks, for example, are semi-public institutions which have considerable and important connections with the Government, and which, therefore, are engaged in a fairly safe business. The Exchange Banks find their principal and most paying business in financing the foreign trade of India. The Indian Joint-Stock Banks attract deposits from chiefly Indians in India and engage in a variety of banking business, too complex to be designated by a single word, but nevertheless meeting a great need. And the local shroff, who is a money changer and a money lender combined in one, acts also as the middleman between the Banks in India and the vast trading community in the whole of the Indian continent. But this apparent specialisation should



not be emphasised too much. Banks of all descriptions endeavour to get into touch with the trading public of India. They must, therefore, necessarily try to take up always some new business. As banking business comes to be more clearly understood in India, as competition becomes more keen this apparently simple scheme of division will have to be abandoned. We find Exchange Banks for instance anxious to attract deposits in India and take their share in financing the internal trade of India. We find the Presidency Banks eager to evade the rigid provisions of an antiquated enactment which prevents their development in all healthy directions. Under these circumstances it would be misunderstanding the character of the Indian money-market if we assumed that there is any division of banking establishments into water-tight compartments according to the class of business they habitually or principally engage in.

To those who are advocates of specialisation in business-as being the only way to a full and free development-it may be an occasion for sincere gratification that the Indian banking community, even in its infancy, exhibits signs of specialisation. And, we must admit, if by any such means exclusive attention of a certain number of banking houses were paid to one kind of business only, and each kind of business were to be similarly attended to, the industrial and commercial development of the country would proceed very rapidly. But a premature specialisation almost

invariably has the defect of one-sidedness. The most paying lines may be cultivated and the rest comparatively ignored, with the result that the country as a whole suffers, and even banking enterprise itself would be lacking in that soundness which is indispensable. This is all the greater when there is no co-ordinating agency to keep in line the various specialised units. With such an institution at the head of the money-market—as the Bank of England or the Reichsbank—we could advocate as much specialisation as we liked; for such an institution would gather in its own hands—silently and imperfectly but none the less securely—all the reins of the country's finance; and by a slight pressure could bring about the correction of the waywardness of any one member of the class. But in India we have no such controlling agency. We shall revert in a later chapter to the need of such an agency in the shape of an Imperial Bank. Here we must observe that in the absence of such an institution, the apparent specialisation in our banking business can only be a source of weakness to themselves and loss to the country. For such a specialisation would on the one hand leave some very important and profitable lines of business almost entirely neglected, and on the other, by compelling the banks to deal more or less with the same people and at last to encroach upon one another's preserves, make them very weak in periods of a general panic.

The extent of the connection between the various classes of existing banks is difficult to deter-

mine precisely. Even if we make only two broad divisions of these institutions—the native and European, we can hardly say to what extent rates in the one govern those of the other, or how readily money flows from one to the other. In the earlier days, perhaps, the connection was very slender. A letter in the report of the Fowler Committee of 1898—from Mr. J. H. Sleight, Secretary and Treasurer of the Bank of Bombay,—says, “During the last export season shroffs’ 60 days’ sight bills were not obtainable over 8 per cent discount—. This was the rate then ruling in the native bazaar both in Bombay and Calcutta, and that, too, while the Exchange Banks were greedy to receive fixed deposits for short periods at 9, 10 or 11 per cent per annum, and while the Presidency Banks were straining to meet the demands for loans at 12 and 13 per cent per annum. But there is no singularity in these facts. The same peculiarity has shown itself over and over again during periods of financial pressure, and even at the present moment (November 1898) while money is not by any means tight there exists a difference of 2 per cent between the bazaar and the Bank rate”. Whether such a state of things exists even today we have no official means of knowing. But, it may be assumed, that as the native banker understands more clearly the methods of the European banker, so will the competition between them become greater and this wide divergence in rates tend to disappear. Nor can we rely altogether on this discrepancy between the bazaar rate and the Bank rate to prove

that the connection between the purely Indian Banks and the European banking houses in India is very slight. For it is well-known that even with the Presidency Banks the published rate of discount is not always the rate they charge on all their advances. If the business handled by the Indian and the Exchange Banks is essentially different and involves different risks the discrepancy in their rate of discount is easily explained. Moreover it is a significant fact—as Mr. Sleight himself mentions in the letter referred to, “I have ever found that when the official rate rose abnormally high, the rate in the native market did not respond to the full extent, but generally stopped at 7 or 8 per cent, though the Presidency Banks’ rate might rise to 10 or 12 per cent. The explanation,” the writer adds, “is very simple. The shroffs, who finance the whole of the internal trade of India, rarely, if ever, discount European paper and never purchase foreign or sterling bills. Neither do they lend on Government or similar securities, but confine their advances to discount of Hoondies, to loans to cultivators, and against gold or silver bullion”. While the two rates often differ the difference is never very great, and is always easily explicable.

(2) From the foregoing remarks we may conclude that the kind of business handled by these various classes of banks is different only on the surface. And this leads us to another characteristic of banking in India. All these institutions



being engaged—or professing to be engaged in banking as it is understood in England,—that is to say, short term loans amply secured with a relatively low rate of interest and rapid turnover,—there is no institution or class of persons whose business it is to promote banking among the people by guiding them in the choice of investments. The banker as a professional adviser to a client seeking investment does not exist in India. On the one hand this results in a complete divorce between banks and industry, the banks being essentially and almost exclusively commercial banks, avoiding industrial financing as a thing to be dreaded. On the other it leaves the investing public without any light or help, a prey to the wiles of speculators in industrial securities, or condemned to profitless habits of hoarding, or a resort to the savings banks. We shall return to the first of these in a later chapter where we deal with the need for an Industrial Bank for India, somewhat on the model of similar banks in Japan and America. In connection with the latter we may mention that a glance at the growth of the Savings Banks Deposits, and of the capital invested in industrial concerns, is enough to show that Indians are waking up to the wastefulness of hoarding, and are trying more and more to seek profitable employment for their savings. But there is every risk of such would-be investors being frightened away from the market by the failures of important banks-of the kind we had some three or

four years ago-but much more so by the risks of industrial investments. We can never develop our industries as fully as we would desire-as the country's resources would permit, so long as we have not enlisted the active sympathy of local capitalists, no matter how small their contributions may be. And we can never hope to arouse the local capitalist so long as our existing industrial securities are, in the three or four centres where there is a highly developed market for them, quoted at prices out of all proportion with their intrinsic value. In the share-markets of Bombay and Calcutta it would be quite true to say that speculative frenzy often reigns and reason seldom governs. If we cross-examine some of the biggest dealers in these securities, if we question even the professional broker, we are sure to be astonished at the absence of any convincing or even arguable explanation for the fluctuations in the value of any security. "Tata's would go up" or "Telephones would go down" or "Mills must fall" not because of any internal advantages or difficulties of these concerns, but because "Mr. Ramchand is cornering them" or "Mr. Pestonjee has sold them" or "Messrs Smith & Company's manager said so." These reasons may suffice for those initiated in the mysteries of the gambling den which works in full daylight with impunity under the name of the share-bazar; but they seldom have any affinity with the real state of those concerns as evinced whether by their balance sheets or their known record in the past, or the changes

in the obvious factors which affect the production or sale of their commodities. And if those who are trained enough to make their own conclusions on the available data—required by law to be published, are often bewildered by the vagaries of the share markets, what shall we say of the ignorant, inexperienced investor of an up country station? However pernicious the action of the professional, respectable gambler may be, the law, it seems, is powerless to check him. But if we do not wish for ever to alienate the small investor—and the success of the great War Loan of 1917 shows beyond any doubt what potentialities there are in India from our nascent industries,—we need very urgently the growth of a new kind of institution which would, for a very small remuneration, furnish the best professional advice to would-be investors. If scientifically trained men of unblemished reputation would undertake the task, and succeed in reviving and promoting general confidence in one's neighbour's commercial honesty, they would do far more to fight and vanquish the rampant speculation in the stock exchanges of India, than any amount of legal enactments or pulpit condemnation. If shares in an industrial concern come to be valued as they ought to be valued on the results of the concern's working coupled with an estimate of its possibilities, if the agents of such concerns are shown their gross error when they speculate in their own shares instead of doing all they can to control those other material factors which deter-

mine the success of their enterprise, the investing public in India would soon rally to the cause of India's industrial regeneration. This can never be done so effectively as by an Investors' Information Bureau conducted by trained men of untarnished reputation. And if this is done the development of banking habits, and consequently the success of banking business, would only be a question of time.

(3). Side by side with the necessity of a special agency to guide intending investors in order to feed the industries of India, mention may also be made of the need for a totally different kind of banker from the one we are at present accustomed to in this country. This need is all the greater because it is not obvious at the first glance. We have already indicated that the terrible collapse of banks in 1913 was in a great measure due to the ignorance and inexperience of the directors and managers of the new institutions, if not to their criminal mismanagement. Apart from the native shroffs, with whom banking business is a ancestral occupation, and who are great moneyed men themselves, the Indian manager of the Europeanised Indian Bank is often sadly lacking in theoretical knoweledge of banking business. Without any general education, without any experience of the business in hand, he soon finds himself in difficulties in dealing with applications for advances ; he is also confronted with the greatest temptations, and it is not surprising that the lessons of past failures have



left little impression on him, and that he often succumbs to these temptations. In order to make money he cares very little what means he employs, perhaps he has never been taught the responsibilities of a rich man. We cannot expect such a man to develop his business in all its branches, and to take a view of his business fifty years beyond his life time. No wonder, then, that the slender measure of success which has so far attended the efforts of Indian bankers is in part—a large part—ascribable to their own character.

So far, however, the situation is not materially different from that in any new country which is pulsating with all the consciousness of life and its immense possibilities. But even the English banker in India, who not infrequently is taken as a model by his Indian confrere, is not always all that can be desired of a banker. He has, no doubt, a greater experience of banking routine than his Indian rival, because he is a man who has served his apprenticeship in a bank in Europe. Possibly he has had a course at the Institute of Bankers and even passed its examinations. But he is lacking as much as the Indian Banker—in that superior realisation of the nature and object of banking, which alone can minister to the financial ascendancy of a country. Nor can he be expected to have exalted notions of his calling. He is only a servant after all. The circle he moves in is pervaded by the dominating idea of making money, and he is soon, easily, affected. It is an open secret in the

money-market how sometimes X the manager of Bank A speculates in the name of his personal assistant in the shares of a company and how Y the Secretary of the Bank B gambles in cotton. That neither X nor Y is easily found out speaks, indeed, highly for the perfection of his education in so conducting his operations as to leave hardly any evidence that could be accepted in a court of law.

Unless this state of things is changed we can hardly expect Indian banking to develop at all rapidly.

(4) So far we have confined ourselves to the characteristics of Indian banking of more or less a general kind. Coming more to details we observe that one great aid to banking development is sadly neglected in India. The table appended herewith shows that compared to other countries, India has not got banks at all in proportion to her population or her commerce, and that such banks as she has, ignore the importance of a wide-spread well-planned system of branches.

# Comparative Position of Banking in some Important Countries.

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Name of the Country.	Population according to the last census in thousands.	Foreign Trade for the year 1914 in thousand sterling.	On December 31st, 1914.			
			No. of J. S. Banks.	No. of Branches.	In thousands. Paid up Capital and Rest.	Deposit and Current Account.
United Kingdom.	45,370	1,222,830	57	7,832	£134,062	£1,257,720
Canada ...	7,206	233,275	22	3,159	45,578	£228,800
U. S. A. ...	91,972	844,721	14,598	Not available.	164,457	£655,554
India ...	315,156	213,000	56	204*	8,084†	£59,033‡

N. B.—Foreign currencies converted at approximately pre-war rates.

\* Approximate.

† Excluding the Exchange Banks.

‡ Excluding deposits held by the Exchange Banks out of India.

Without a good system of branches we cannot expect banks to tap all the possible sources, to draw out the hoarded wealth of India—if any there is—and employ it in the cause of industry. Of late there has been a welcome addition to branchification in the case of the Presidency Banks. But on the whole the branches as they exist are utterly inadequate.

(5) Another suggestion that the existing practice of banking in India imperatively demands is in respect of the cheques. It is true the cheque system cannot make any great progress in an illiterate country like India. But even in this country, if the cheques were allowed to be drawn—in a set form—in any language familiar to the customer, we are confident of an appreciable progress in the use of cheques even under existing conditions. And if to this were added a reduction of the stamp duty upon a cheque, the increase would be still greater. The latter suggestion, we admit, is at first sight opposed to the English practice since the existing stamp duty on cheques is the same in India as in England. But if we bear in mind that the average English cheque is drawn for a much larger sum than the average Indian cheque the incidence of the stamp duty would be found to be relatively greater in India. We make this suggestion at some length because the greater use of cheques would, in our opinion go a great way in solving such currency troubles as those we have had this year.

Other suggestions—such as the principles of advances, the mode of attracting deposits etc.—



could be made with regard to the internal routine of a banking house; but neither the scope of this work is so wide, nor the experience of the authors so intimate as to allow them to insert all these. Suffice it to say that there are great possibilities for banking in India, that at the same time there are serious drawbacks in the organisation and management of banks, and that only when those drawbacks are removed can banking—and consequently the commerce and industry of India—develop as fast as can be desired.

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## CHAPTER IV.

### **Some special kinds of Banks in India.**

In the preceding chapter we have endeavoured to sketch the general organisation of the more important commercial Banks in India. These, however, do not exhaust the list of banking and credit institutions of India. Mention was made in the last chapter of the apparent specialisation in the existing commercial banks with some show of trying to finance a particular section of the trading public; but we showed how the appearances were delusive and that these banks in reality all transacted much the same business. In this chapter we shall attempt to describe the organisation of some other banking institutions which are undoubtedly meant for, and which strictly confine themselves to, the special object with which they were instituted. So much, indeed, is their specialisation that it may even be doubted if the designation of a bank is at all appropriate in their case. If, however, we regard the development of credit as the prime function of all banking institutions, we would have no difficulty in classifying the institutions described below as banks. But if we are to appreciate them rightly, if their constitution and working is to be properly

understood, if their development is to be promoted on the correct lines, we cannot but lay stress on the specialised nature of these bodies at the very outset of our discussion.

## I. CO-OPERATIVE CREDIT SOCIETIES.

The most important of such institutions are the Co-operative Credit Societies. It would be beyond the scope of this work to go at length into the history of the co-operative movement in India. Suffice it to say that the abject poverty of the people of India intensified still more by their heavy indebtedness, coupled with their dependence on one calling-agriculture-makes India an extremely fruitful field for the co-operative principle; and the perception of this led to efforts—at first isolated, afterwards co-ordinated—which resulted in an Act of the Government of India instituting these societies. The original Act of 1904 was modified substantially in 1912, so that to-day Co-operative Societies may be formed for the development of credit—or other purposes by any ten persons living in the same locality or belonging to the same class. The main business of a credit society is to raise funds by deposits from members, loans from non-members, Government and other co-operative bodies, and to distribute money thus obtained by way of loans to members, or, with the permission of the Registrar, to other co-operative societies. The principle of unlimited liability of members for the debts of the society, and the idea of gratuitous service and indi-

visibility of profits were at first universally enforced, and are even now the basis of by far the largest number of the credit societies. Government gave no assistance to the societies as such at their outset, but they reserved to themselves certain powers of control *e. g.* the audit of their accounts by Government Inspectors, or the general supervision by the Registrar of Co-operative Societies in each province.

A credit Co-operative Society—chiefly agricultural—is usually constituted by inhabitants of a village enrolling themselves as members. Each of the member takes one or more shares—the limit of holding by any individual member is fixed—if the capital is made up by shares; and, if there are no shares, by a small admission fee. The supreme power in the society is vested in the general body of the members who—at the annual general meeting—elect the Managing Committee, fix the borrowing powers of individual members, as also those of the Managing Committee, dismiss members for misconduct and settle the rate of interest. The government of the society is entrusted to a Managing Committee, consisting of from 5 to 9 intelligent members elected by their fellows. The chairman is generally the leading personage in the village. The business of the Committee is to admit new members, to receive deposits, to arrange for outside loans, grant loans to members, and take notice of defaulters. The routine work is conducted by the Secretary, who, if he is a bonafide member



of the society, gets a monthly pay of Re. 1 to Rs. 5 with a bonus at the end of the year equal to a fourth of annual profits. He keeps the books of the Society according to rules framed by the Local Government, on forms and papers supplied by the Registrar. As the duties of the Secretary require considerable amount of education, the village Societies are often put to it to find a competent man for the task, and they sometimes solve the difficulty by combining together and employ a salaried official to discharge these duties. The village school-master or accountant is not infrequently the most competent person at hand, and if he is a member of the local society, no difficulty need arise. But as the work of the societies develop the need for a trained Secretary would be felt more and more, and the experiment, like the one tried in Bombay by the Servants of India Society with the active support of the Registrar of Co-operative Societies in Bombay, for the training up of secretaries needs to be more generally attempted.

The funds of these societies are derived chiefly from deposits. They may—and sometimes they do—raise a portion of their working capital by means of shares or membership fees; but as the average member can but ill spare considerable amounts for payment of shares, it has almost always been necessary to allow these payments to be spread over a number of years. Deposits, thus, constitute an important part of their working capital. Some

societies insist on compulsory deposits from members ; but the plan has too many obvious disadvantages to be generally acceptable. Hence though a part of the working capital is obtained by deposits from members and local sympathisers, by far the larger portion is obtained by means of loans from other Co-operative Societies and from the Government. The Government in all the Presidencies set apart every year a certain sum to be advanced as loans to newly started Co-operative Societies, usually an amount equal to members' deposits. But State aid in the form of pecuniary doles is now so generally condemned that it is rather the exception than the rule. But the place of Government loans is taken by assistance from central banks. Since Co-operative Societies lend to persons from whom they could not expect to realise their investments at a short notice, they could not expect any financial assistance from the ordinary commercial banks. And if Government aid was also to be discountenanced on principle, the problem of financing these institutions becomes at once very serious. The problem was first solved in Madras by a Central Co-operative Bank, which advanced money to the primary societies, and which was started as early as 1907 without Government aid. In other provinces District Banks were established soon after with the same object. These banks have a large share capital and this enables them to attract deposits for fairly long periods and also to borrow occasionally on reasonable terms from the ordinary

commercial banks. They advance the money thus borrowed to the primary societies with a small margin of profit. The working capital, therefore, of these societies may be derived from shares, members' deposits, outside deposits, outside loans from individuals or societies, State loans and the Reserve Fund. The several items are represented by the following figures in the latest report :—

Shares	...	...	Rs. 65,00,000
Members' Deposits	...	...	33,00,000
Loans & Deposits from non-members.			37,00,000
"	"	" other Societies.	2,68,00,000
State aid	...	...	11,00,000
Reserve Fund	...	...	38,00,000

The business of these societies is to make loans to members with a view to prevent them getting into the clutches of the money lenders. The loans according to the underlying principle of co-operative movement, are made on the personal security of the members; but under the Indian law on the subject the societies are allowed, under certain conditions, to make loans on the hypothecations of movable or immovable property as collateral security. For long term loans, and loans for the liquidation of old debts, the societies usually take a mortgage, though in the best interests of co-operative banking this tendency, which has not always been kept within bounds, ought to be discouraged. Thus in Madras the percentage of loans secured on mortgage in 1913-14 was 47, in

Bombay 43, in Burma 36, and the average for all the provinces was 14. The profits of the societies are carried to a Reserve Fund which is indivisible and which is invested in the manner prescribed by the Registrar. This fund is intended to meet unforeseen losses and is also a security for loans. The practice is common in Madras and the Central Provinces to use this fund as part of the working capital, but the better informed opinion is against that practice.

After this general sketch of the organisation and working of these societies, we may proceed to give some figures to illustrate the progress of the movement.

Year.	No. of Societies.	No. of Members.	Working Capital.
			Rs.
1904—5	41	...	1,54,120
1905—6	283	28,629	4,73,220
1906—7	843	90,844	23,71,683
1907—8	1,357	149,160	44,14,086
1908—9	2,008	184,889	80,65,111
1909—10	3,498	230,698	1,23,91,682
1910—11	5,432	314,101	2,03,66,584
1911—12	8,177	403,318	3,35,74,162
1912—13	12,324	573,536	5,34,34,261
1913—14	15,673	744,226	7,71,70,584
1914—15	16,324	824,469	8,96,61,722
1915—16	19,675	918,436	10,32,67,149

So far we have confined ourselves to giving the barest sketch of the existing organisation of the



Credit Co-operative Societies, without in any indicating the problems which at present face the advocates of this movement. We shall now turn our attention to discuss briefly the obstacles which the co-operative movement is now meeting with, and suggesting, if possible, some solution. (1) The problem of management is one of the gravest that the movement is meeting with. The co-operative principle precludes the possibility of employing paid outsiders with the necessary qualifications; and under the existing state of things to expect any of the members to take up these duties would be futile in most cases. The only man in the ordinary village society of today who could at all transact the business of the co-operative society, is the village money-lender. But for good or for evil he is the one man against whom the co-operative movement has set its face. It is, indeed, true that the first object of the movement is to free the Indian cultivator from the heavy burden of accumulating debt to the local money-lender. The latter, therefore, sees in the growth of the co-operative movement his own mortal enemy and naturally does all he can to thwart it. They would be mistaken who assume that the village Mahajan has even now lost his influence. The villagers do not always see that in the long run his rate of interest works out at a very heavy figure; but what they can and do understand is that the Bania is always at hand, that he is ready to advance money, can appreciate the importance of the occasions for which they have

to borrow, and would dispense with every wearisome, unintelligible, formality at the time of borrowing. And even in regard to the time and manner of repayment, the Mahajan is always willing to grant an extension. In all these respects the Takavi advances from the Government are entirely unsuitable to the cultivatory, and they, therefore, preferred the usurious loans from the Mahajan to the cheaper ones from the Sircar. The Co-operative Society now comes upon the scene with its open challenge to the Mahajan. But even the Co-operative Society requires some formalities, which, however simple, are sure to be wearisome to the illiterate and the needy. The society, also, does not always advance loans freely on any and every pretext. The local money-lender, therefore, still retains his influence. And the success of the Co-operative movement would be greatly facilitated if the assistance of the Mahajan can be enlisted in its behalf. That this assistance would be extremely valuable is obvious. The villiage money-lender is the only individual in that simple society with any experience of banking, with any knowledge of accounts; and the primary credit society needs badly some one to conduct its banking operations, to look after its accounts. How to make him co-operate with the village society is indeed the most serious problem. To bring him in as a predominant shareholder, or even to associate him with the society as a paid official would make the society—quite conceivably—lose sight of its original nature

and object. To leave him out altogether is to invite the most formidable rivalry.

If the co-operation of the Mahajan cannot or ought not to be had, the only alternative for the societies is to employ a paid official for the management of their concerns. The question of payment calls forth some hostile criticism not only because it is essentially opposed to the co-operative principle, but also because the average society can ill afford to pay a competent full-time official his reasonable remuneration. The latter objection has, indeed, been met in some measure by the voluntary grouping together of a number of primary societies which may together be able to bear the charges of a well-paid official. But this grouping is possible in the case of only those societies which are situated within reasonable distance from one another. And even so the employment of a paid official is against the co-operative principle. The only safe method, of course, is all round education ; but in the absence of that education the strict rigour of the co-operative principle would have to be modified.

(2) Another equally important problem in connection with the co-operative banking in India is about their finance. They cannot, of course, hope to raise the required funds from among themselves either by deposits or by shares. The system of shares is, indeed, objectionable in their case as its inevitable implication would be a division of profits and the consequent commercialisation of the con-

cerns. Co-operative Banks cease to be co-operative when their directors are encouraged to estimate their success by the rate of dividends. The issue of a share capital is permissible only when the area of a bank's operations is very extensive, when the members cannot be expected to know everything about one another, and when they would be unwilling to shoulder unlimited liability for strangers. And as regards deposits, these banks could not expect to raise considerable sums by way of deposits from members who are more likely to be borrowers than lenders. The societies must, therefore, depend for their working capital on outside aid. Deposits from private individual sympathisers from outside are an important source of working capital, and loans from such sources are still more so. But the question of such loans is complicated by the requirement of security. The societies—apart from their reserve fund, have no security to offer for the loans they raise. It takes, however, years to build up a considerable Reserve Fund. The joint personal credit of the members is thus the only security the societies can offer for their loans. And as a good many of the members are heavily indebted, such security is never very valuable in the eyes of the ordinary commercial banks. The principle of financial aid by the Government has been too definitely discountenanced from the beginning to be at all important. Hence the question of finance is extremely complicated. It has been solved in part by the formation of central societies which by co-ordinating the assets



of its members might be able to help each one in its need, and if more aid is wanted such a central society can obtain it more easily from the ordinary money-market than each individual society. On this ground it is urged that the movement in favour of central societies should be further encouraged by the formation of Provincial Co-operative Banks, which can on the one hand borrow the surplus funds from the ordinary money-market whenever possible and needed on the best available terms, and lend the same on the other hand to the central societies at rates of interest which would leave a sufficient margin to meet their own expenses. We believe, therefore, that the formation of Central Provincial Banks, culminating in a branch of a Central Imperial Bank would solve effectively the problem of financing these novel institutions.

(3) The next important problem in connection with these institutions is about the object for which loans could be advanced, and the security that should be asked for these loans. To take the latter first the ideal of the co-operative movement is always to seek personal security. If the habits of thrift are to be inculcated, if the load of indebtedness is to be removed, personal security would prove in the long run to be the best security that could be desired. On the other hand the average borrower from such societies is so poor and so heavily indebted already that his own bond would be hardly enough for the prudent banker. The difficulty here is caused

by the conflicting claims of prudent banking and co-operative credit. If collateral security is needed, the only one that the usual borrower can offer is his land; but the ultra cautious banker would look askance at all forms of mortgage of real property as collateral security. The permission, which is now given in some cases, to accept the hypothecation of real or personal property as collateral security, is only a confession of the inability to solve the problem in a way to satisfy the dictates of prudence and co-operation. We may take it, however, that as the spirit of co-operation gains ground, as its nature and object becomes better understood, personal security by itself would suffice to the most exacting manager of a co-operative credit institution.

As regards the objects for which loans may be made by these societies to members—they cannot advance to outsiders unless they also form another Co-operative Society—the most laudable would of course be to utilise the funds thus obtained in improving the holding of the borrowers. But that is possible in the case only of a fairly advanced and educated members. The more common request for accommodation is from members desirous of meeting ceremonial expenses—which they consider inevitable, or to pay off old debts. Both of these are unproductive objects and to lend for such objects is, it may be conceded, to encourage the habits of thriftlessness or waste. But as these expenses on ceremonial functions are, from the point of view of the borrower, inevitable, unless the society advances money, the

member will go to the money-lender, and undo the work of the co-operative society. Not to lend then on such occasions would be to play deliberately into the hands of the most formidable rival of the co-operative movement, and thereby defeat its own purpose. But nothing can be said against the practice of lending and yet discouraging such borrowing in future by every means in the power of the society. So also in the case of the old debts. The member who is clear-sighted enough to perceive the wastefulness of the old debts incurred from the money-lender must be given every facility to carry out his object. If the society helps him in doing so it would no doubt substitute its own debt for that due to the money-lender; but as its loan would carry much lower rate of interest than that of the money-lender, the practice would be commendable from every point of view. Of course such facility must be cautiously given, and only to people who would not abuse it. And if it is advisable to keep up the spur to the borrower's thrift and industry by the salutary fear of a steadily menacing debt, the society can only offer itself as a guarantee to the old creditor for the ultimate payment of his debt, and by this means secure better terms for the debtor without removing the spur to his thrift and industry. Hence the co-operative credit society must always grant loans to its members, within the limit fixed by its bye-laws for every object which in the opinion of the Managing Committee, would compel a member to borrow. The society may, indeed,

profitably use its moral influence to discourage wasteful borrowing, but it should not try to prevent such borrowing by a positive refusal to lend itself.

The last point of any importance that need be mentioned in this connection concerns the rate of interest charged by the society for its loans. It is clear, of course, that the society cannot and should not lend below the rate that it pays itself on its deposits or loans. But the upper limit of the rate to be charged is not so clear. The society's object is not to make profits but to help its members. At the same time the co-operative credit society is not a charitable institution. Hence it may be permitted to charge the rate of interest prevailing in the neighbourhood, taking care, however, that such a rate does not end by becoming usurious. If good profits are obtained from such a practice they may be devoted to the Reserve Fund to improve the general credit of the society. In any case the rate of interest should neither be so low as to involve the society in a loss nor so high as to prevent the members appreciating the difference of borrowing from the society and borrowing from the money-lender.

## II. THE SAVING BANKS.

Another class of such specialised banks of which some mention should be made in this chapter, consists of the Savings Banks. They are meant to promote thrift among men of small means by taking care



of their savings and giving them a stimulus in saving by offering a certain rate of interest. These are essentially banks for men of regular but limited means. Public Savings Banks were first established in India between 1833 and 1835 in the Presidency Towns; and in 1870 district savings banks were instituted in connection with selected district treasuries. The Post Office Savings Banks, opened in 1882-1883, absorbed the business of the district savings banks in 1886 and those of the Presidency Banks in 1896. They allow interest since 1905 at 3 per cent on deposits at call, and  $3\frac{1}{4}$  per cent on deposits fixed for 6 months—but this practice has been modified since 1911. Each depositor is allowed to deposit only sums upto a certain limit, the savings beyond which being converted by the Post Office into Government paper at the option of the depositor. The deposits in Savings Banks represent a floating charge on the credit of the Government of India.

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## CHAPTER V.

### **An Industrial Bank for India.**

#### **I. NEED FOR AN AGENCY TO SPECIALISE IN INDUSTRIAL FINANCE.**

We have so far discussed the organisation and working of all the existing Banks. In this sketch it would have been obvious to the careful reader that the banking organisation of India is susceptible of several material improvements. We have ventured to suggest several improvements of detail in each particular instance. We shall now proceed to suggest more far-reaching changes which would vitally affect the organisation of Banking in India, and yet not alter very much the existing system. The creation of a special Bank for Industries would hardly seem to concern either the Commercial or the Co-operative Banks; and even the establishment of an Imperial Bank would at first sight hardly touch the institutions described above. Viewed as a whole, however, and in the long run such creations are bound to have far-reaching effects and we shall, therefore, proceed to make our suggestions in some detail.

The development of industries in any country is necessarily limited by the available capital. In these days of complex machinery and large scale production, even a single factory, if it is to be worked economically and satisfactorily, requires lacs of rupees to start. The first essential, therefore, for the growth of industries in a country is to obtain all

its available capital and to distribute it where it is wanted. It is a truism of economic science that capital is mobile, and that the prospect of higher returns would make it flow from one country to another, provided it is not unusually risky to invest in that country. In this respect, therefore, the acknowledged poverty of India need not lead us to despair. We can offer, thanks to a strong settled Government, the best security for capital that any borrowing nation can offer. We have a vast labour force, untrained it is true, but yet cheap and plentiful enough to convince the most pessimistic entrepreneur about the success of a well-equipped, well-managed establishment. We command abundance of raw material for almost every kind of industry. And the success already achieved by some of our new industries—cotton, and jute, tea and iron,—is enough to give reasonable hopes for the success of others. In spite of all these favourable conditions, however, we are industrially more backward after 60 years of internal peace than many a South American Republic in spite of their ceaseless revolutions. The explanation of this backwardness is to be found among other causes, in the absence of any institution whose sole business it would be, to find out where the capital is in abundance, to attract it to itself and to distribute it as and when our nascent industries require. It is not only that new industries cannot be started for want of capital; but some of the most flourishing and well established industries find it hard in a time of crisis to hold their head above

water when there is no institution to give them a helping hand. The failure of many great concerns can be explained in this way, although other causes too might have contributed their share. Such an institution though seemingly a banking institution, would be essentially different from the banks as we know them in this country. If the existing banks could do the needful, there would be no reason in suggesting another. India possesses, no doubt, a fairly creditable banking organisation; but the principles on which they carry on their business would not permit them to act as purveyor of capital to industrial concerns. In fact, they are insufficient for the needs of those whom they cater. Some of the Indian banks did indeed dabble to some extent in helping industries, but the crash of 1913 has revealed the transactions of some of them to have been of too shady a character to be imitated. Industrial finance is so radically at variance with the ordinary business of a commercial bank that any such institution venturing to carry on both at the same time is bound to come to grief. The large joint-stock banks in India and the so called Exchange banks, have therefore almost always refrained from the business. Even the Presidency Banks, in spite of their semi-public character, are not suited to act as industrial banks. Apart from the restrictions of their charters, which prevent them from entering upon certain kinds of business, but which can be modified, if required, their position in the commercial world would not permit them to deliberately divert



their business at this late hour in a new and at best an untried direction. Moreover, being private institutions at bottom, their management cannot always be trusted to take a view of the industrial possibilities of India which must and will be adopted by those who desire a rapid development of industries in India.

"The problem of Industrial Banking", says the "Capital", is to have banks which can borrow for longer periods, so that they may not run the risk of having their funds withdrawn suddenly, with a staff capable to judge the technical and business prospects of concerns which come to them for assistance."

That a special bank for Industries has a great future can be proved not only from the fact that the existing banking institutions of India are not equal to the task and therefore the proposed Industrial Bank would have a practical monopoly of that kind of business but also because such an institution is badly needed by the small capitalist in India. It needs no confirmed belief in the theory of the hoarded wealth of India to admit that there are people in India who do set aside every year something, who would desire to invest their savings, but who in the absence of any institution to guide them in their quest for investments, are forced to accumulate their treasure or even to bury it, or to resort to the savings banks of the Post Office. It may be said for those who seek opportunities for investment, the newspaper advertisements, and the publication of the prospectuses

by new joint stock enterprises would be enough indication as to where to invest, not to mention the institution of Stock-Exchanges. But the country is so vast that the advertisement in the Bombay papers would hardly be read in Lahore; the bulk of the people are so illiterate and inexperienced in the wiles of the modern company-promoter that the best thing they can do is not to trust to the published prospectuses, and the stock-exchanges are so notoriously the haunt of speculation and sharp practice that we cannot accuse a prudent investor of undue timidity if he does not resort to them.

An important objection which may be raised against the starting of an Industrial Bank is that the existing banks will suffer by unfair competition because the Industrial Bank as suggested having the support of the Government, will be able to attract funds which now form the working capital of these commercial banks. We believe that there is not likely to be any keen competition between these banks and the proposed institution, because, as will be explained later on, the proposed bank in the first place will draw funds chiefly from a different class of people who have not much confidence in the existing banks or who do not consider the interest offered by them sufficiently attractive and advance them chiefly to those who are unable to get assistance from the existing banks. And secondly it will not engage in other kinds of business such as short term deposits or current deposits, remittance of

money, sale and purchase of shares, underwriting of securities, etc., which are carried on by the commercial banks. However, even if it is admitted that the proposed bank will divert funds from the Commercial banks, it cannot be denied that the funds thus diverted will be better utilised than they are now, because if a person deposits his money with a bank, say, for six months, and renews his deposit nine times after the expiry of the period, the commercial bank being not sure of the deposit being renewed, cannot make as good use of the funds as the proposed institution will be able to do by taking that deposit for a period of five years. On the other hand it can be said that the development of industries will encourage the other branches of the business of Commercial Banks.

Under these circumstances, then, there are three reasons for the establishment of a special Industrial Bank in India:—viz (a) the need of our industries both old and the new, (b) the unsuitability of our existing banks for the task, (c) and the interests of our small investor.

## II. METHODS OF ESTABLISHING THE INDUSTRIAL BANK IN INDIA.

This being a specialised institution its creation cannot be allowed to proceed on the ordinary lines of unaided, competitive, private enterprise, for in spite of all its merits, private enterprise is bound to

incline in the direction where there is the highest expectation of net return to capital, in the shortest time. We cannot blame such an institution for that tendency; but we cannot also deny that such a tendency is bound to defeat the object with which this institution should be started. Even if the Directors of the Bank succeed in keeping the bank from becoming a semi-commercial undertaking, they cannot always guarantee that impartial, liberal assistance to new industries without any suspicion or undue bias—which is a prime requisite for realisation of the ideal. We need therefore some sort of Government assistance. This view is supported by the Committee appointed to report on the proposal for establishing a “British Trade Bank.”

Public assistance may be afforded in a variety of ways. (i) Government may subscribe a part of the capital; or (ii) without subscribing any part of the capital, they may yet guarantee a certain minimum dividend on the capital for a given period or under specified conditions; (iii) they may keep a certain fixed minimum deposit with the bank free of interest, and bearing a certain proportion to the capital of the bank; (iv) help to attract capital for the bank by exempting its dividends from the income tax, or remitting monies free of charge from one branch of the bank to another, or from a private individual to a branch of the bank by means of Treasury Remittance Transfers, or by permitting trust monies to be invested in the securities offered by the bank. Of all these



means the first would be open to serious objections both financially and otherwise. If the Government were directly interested in the success of the bank by being a substantial shareholder, the development of the bank as well as of the industries in general would be assured. But unfortunately the current of individualism is still so strong that one despairs of any fair consideration being given to a proposition which savours of collectivism a league off, especially in India where we live in an atmosphere of general distrust. Besides, if private funds can be had for the purpose, it would not be advisable to suggest the locking up of considerable public resources in the undertaking. As regards the second mode of Government assistance there are ample precedents even in India. If private enterprise under public control is to take up this national task it is but fair that, on the analogy of our more important Railway Companies, the shareholders of the Bank be guaranteed a minimum dividend, say of  $4\frac{1}{2}\%$  p. c. per annum. It may be laid down subject to revision after every ten years for instance that the Government would pay a dividend of  $4\frac{1}{2}\%$  if the Bank made no profits, or that they would make up any deficit in that figure, provided that out of the profits of the bank, when earned, a  $4\frac{1}{2}\%$  dividend should be paid first, then one half of the remaining profits should be transferred to the Reserve Fund until it becomes  $50\%$  of its paid-up capital and the other half should be divided, equally between the shareholders of the Bank and the Government. Such a gua-

rantee is justifiable as it is necessary, for this is a business of first-rate national importance. Nor would the guarantee be ruinous to the Government, since  $4\frac{1}{2}\%$  on a capital of say 5 crores would mean a liability of  $22\frac{1}{2}$  lacs a year if the bank made no profits at all. It is absurd to suppose that the bank would make no profits at all even in the first year. The guarantee, while it would secure subscriptions to any reasonable amount to the capital of the bank, would not at all prove a burden to the people in general. On the other hand if the bank is worked properly there is every likelihood of the Government making some profit out of this arrangement, just as is the case with the Imperial Government of Germany on account of a somewhat similar arrangement with the Reichsbank.

As regards the third mode of public assistance to the bank, a certain fixed deposit from the Government would not only add to the working capital of the bank, but it would bring that confidence in such undertakings which is sadly needed in India. For example if the public deposits are equal to the total capital of the bank, say 5 crores, the Government can easily find such a sum from a variety of sources. We need but mention the cash balances in India and in England and the various Reserves to show the practicability of the suggestion. The remaining modes of public assistance are calculated to bring ever increasing profits and business to the Bank. The policy of exempting profits of certain con-

cerns of National importance has been pursued by Austria-Hungary and the concession of transferring funds from one city to another is given already to Co-operative Banks and Societies in the Punjab.

As a compensation for that aid we may have a measure of Government control. In the case of a new venture like the one under consideration public control, to a certain extent, is needed also for creating confidence among the people in such an institution. However we must add that the Government should avoid interference in the working of the Bank as much as possible.

### III. THE ORGANISATION OF THE INDUSTRIAL BANK.

The most difficult question of finance being thus solved, the next point to consider is the organisation of the bank. There are two alternatives: viz. to establish an independent industrial bank in each important province, or to have a single central institution for the whole of India with branches in all the important centres. The first would appear to be commendable inasmuch as the needs of each province vary and can be provided for by a local institution more efficiently than by a distant central bank. Without, however, denying the immense diversity in local conditions, it may be said that the industrial needs of the country as a whole, require that such an institution should be a central one. With independent unconnected provincial banks, we

would have no guarantee against waste, while with a single central body, which is obliged to have branches in all important centres, we can have the double advantage of economic management as well as a proper attention to local needs. The other advantages in favour of an All India Industrial Bank are (i) that on account of having much larger capital than any of the Provincial Industrial Banks, it will inspire greater confidence, and (ii) it will be able to use its funds better. Such a bank should, at its very start, have the ideal before it that though a central body itself, it is in duty bound to afford the requisite banking facilities to every province. The extension and multiplication of the branches of such an institution is necessary not only in the interests of the industrial centres of India, but in the immediate interests of the Bank itself. For with its many branches it would be able to tap the savings of as many centres or more, and direct them into unexplored, yet profitable, channels.

#### IV. BUSINESS OF THE BANK.

To put it very briefly we suggest that the Bank should be allowed to do the following kinds of business:—

- (1) To borrow money by means of deposits payable within not less than two years and by the issue of Bonds or Debentures payable after 10, 15 and 20 years.



- (2) To advance money to industrial concerns already existing or coming into existence against first mortgage of their building, plant etc. and liquid assets.
- (3) To place industrial securities such as debentures of Industrial concerns on the market with or without its guarantee.

#### V. THE WORKING AND MANAGEMENT OF THE BANK.

The Bank once started in the way described, the question of its working and management is relatively easy. The general policy of such an institution being one of national importance, should be entrusted to a body of men who would combine business experience and commercial caution with the wide outlook and national sentiment of statesmen. It would, therefore, be best if the Board of Directors of the Bank consist of the representatives of the shareholders—with as many seats as all the other Directors put together—the representatives of the public nominated by the Government, and the representatives of such important industrial bodies as fail to find seats either by election by the shareholders or by nomination by the Government. The Board so constituted should deal with those questions of general policy which affect the industrial development of the country at large, and in which the Bank's aid is demanded. It would be a question of general policy for instance whether the bank should hold any, and

if so what, shares in an industrial concern like a shipbuilding yard in India, or what securities it should accept in general, or what should be the normal length of advances, or how to attract the savings of the people. Questions of minor policy, e. g. the amount of advances to individuals should be dealt with by a smaller committee of the Board, appointed by them to assist the General Manager of the Bank. At the central office in each province there should also be such an advisory committee of the provincial notables appointed to aid, advise and, if need be, to check the provincial manager.

The reasons for all these suggestions are obvious. Public representation on the Board is necessary not only to provide the outlook of the statesman, but also to safeguard the interests of the public. The Government would be very much interested in the success of the Bank both for its guarantee and for its deposits. Special interests require representation since the Industrial Bank cannot be regarded as a mere private commercial venture. A Managing Committee is needed both to check the General Manager as well as to dispatch business since the whole Board of Directors cannot be expected to meet more frequently than once in a month, they being presumably residents of different provinces.

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## CHAPTER VI.

### **A State Bank for India.**

#### **I. HISTORY OF THE SCHEME.**

To the report of the Chamberlain Commission is appended a long memorandum by Mr. J. M. Keynes on the need of a State Bank in India, its constitution and functions, its advantages and disadvantages. This was, however, not the first time that the proposal was made. Proposals for starting a Central Bank were made even before 1860 as we find that in his speech, delivered on the occasion of introducing the bill for the establishment of a Paper Currency Office in India, Mr. Wilson, the first Finance Minister, expressed his opinion in favour of the same. In March 1867, when the old Bank of Bombay was known to have lost a large part of its capital, a scheme was submitted to the Government of India for the amalgamation of the three Presidency Banks into a Central Bank for all India with a paid up capital of five crores of Rupees and an unpaid capital of the same amount. Although the resolution in favour of the amalgamation was carried at a special meeting of the shareholders of the Bank of Bombay, the opposition was so strong that the directors of the Bank, not feeling sure of its being passed at the second special meeting, suggested to the Directors of the Bank of Bengal a withdrawal of the scheme which was done. Some thirty years later some witnesses before the Fowler Committee of

1898-99 advocated the establishment of a Central Bank in order to enable the Banking resources to keep pace with the growing requirements of the country. A member of that very Committee, Sir Edward Hambro, in a separate note appended to the report of the Committee, drew attention to the fact that it had been considered wise in Europe to entrust the carrying out of Currency laws to special Banks established anew, or subsidised, for the purpose. The Bank of England is entrusted with the entire management of the Paper Currency in England—and also of the Gold Reserve. On this analogy Sir Edward went on to suggest the foundation of some such institution in India, planned on the model of the Bank of France. Lord Curzon's Government at first took up the idea, but Sir Edward Law—the Finance Minister who succeeded Sir Clinton Dawkins, could not approve of the proposal, which, therefore, was suffered to drop. For ten years or so it remained in abeyance until revived by Lord Crewe, who authorised Sir Lionel Abrahams of the India Office to draw up a considered memorandum on the subject. This was presented to the latest Commission on Indian Currency, and the latter decided that the whole subject should be investigated by a special committee before any steps could be taken by the Government.

## II. GROUNDS FOR THE SUGGESTION.

Turning now to the need for an Imperial Bank for India, let us first examine the reasons which require such an institution. (1) In the



first place the artificial system of Indian Currency requires considerable management. If the exchange value of the rupee is to be maintained at 1 s. 4 d. both in England and in India, the authorities must be prepared to give gold for rupees and *vice versa* according to the state of trade. This action by the Government gives the whole system an aspect of undue management, not only because the Government's own obligations outside India might expose them to the suspicion that they may manage exchange to suit their own objects; not only because in the one or two crisis in which this system has been tested during the seventeen years of its existence, the public found the system wanting, but because in the hands of public officials such a system can never work with that automatic precision which it would easily acquire in the hands of a bank with wide trade connections and in complete touch with money markets of India. It may, indeed, be suggested that this is not an argument for establishing an Imperial Bank but rather for abolishing the present system of currency. But even if the present artificial position of the rupee was dropped there would still be strong reasons for the creation of an Imperial Bank.

(2) Our Paper Currency system has been based on a principle which in itself is not adaptable to the changing conditions of trade. But Government issuing paper currency as a public monopoly cannot very well abandon a principle which ensures the prompt discharge of obligations even at the risk of inelasticity. Public credit must be maintained

absolutely unimpaired at any cost. But on the other hand the trading community is bound to suffer from a system which, originally meant to help them, now regards their needs of altogether secondary importance. These conflicting requirements of immediate convertibility and easy elasticity can only be met by an institution which has the confidence as well as the resources of the whole nation at its disposal. And this need would remain whether our currency notes are convertible in silver or gold. (3) Apart even from the requirements of the Paper Currency the establishment of a State Bank would be necessary—if for nothing else—to deal satisfactorily with the Cash Balances of the Government. We have already criticised in a previous chapter the wastefulness of the practice which locks up huge sums of money in public treasuries, often at times when the business world badly needs every rupee that can be conveniently spared. But, unfortunately, the tradition of Indian finance which requires considerable balances to be always maintained has now acquired the strength of an irrefutable maxim. He would be a bold Finance Minister in India who budgets deliberately for a deficit, though an outside critic often wonders if such a minister is not badly wanted once in a way. Under the circumstances—if the Finance Minister goes on budgeting for surplus and economic theory goes on demonstrating the wastefulness of such a practice—the only way to reconcile an Indian Financier and an theoretical economist is

to set up a body which would permit—would even encourage—the financier to pile up the surpluses, and which at the same time would pacify the economist by turning that money to account as fast as it is being poured into the Treasury.

(4) These reasons, each grave in itself, are all intensified by the inexperience of the men at the head of the Indian Finance Department. The conditions of public service render frequent changes inevitable, and in spite of the fact that the management of the finances of a country is a highly complex subject, requiring long and patient study, hardly any man who counts in the department remains at his post for more than five years. Scarcely has he come to understand his work than he has to go on to another post perhaps in another province. And, then, the work of co-ordinating the various kinds of banking institutions, and thereby promoting the industrial, commercial and financial development of the country, can never be done successfully by the State as a State. An Imperial Bank on the other hand would, by having several specialised departments, each in relation to particular kinds of Banks, be able to minister to the needs of all.

### III. POSSIBLE OPPOSITION TO THE INSTITUTION.

On the other hand it is just possible that the institution of an Imperial Bank might be resisted by the existing Banks. The Presidency Banks might well apprehend from such an institution the loss of



the public business which they are now able to get. We may take it, however, that that proportion of public business to the total business of the Presidency Banks is so small, and the restrictions upon their operations are comparatively so hard, that the far-sighted managers of these banks would probably be inclined to welcome the institution of the State Bank, if, by sacrificing a part of their business, they get liberty to develop what remains in every way they can. It is, of course, a totally different question whether the Presidency Banks should not themselves be amalgamated to form a State Bank. We reason on the supposition that the proposed State Bank in India would be an altogether new institution leaving untouched the existing institutions. Almost the same reasoning may be adduced in connection with the probable attitude of the Exchange Banks to the new creation. At first sight it would seem that if the Imperial Bank or the Presidency Banks are allowed to engage in exchange business, to attract deposits and borrow money outside India, they—the Exchange Banks—would suffer. But the practical monopoly of the exchange business which these banks have, is far too deep rooted to make them apprehend a serious diminution of their business. In all probability neither the proposed Imperial Bank nor the Presidency Banks, freed from their present restrictions, can expect to do much foreign exchange business in the first few years; and if at all they do acquire a share of that business, this share would be more the



result of a normal increase of business than the fruit of a keen competition with the Exchange Banks. On the other hand the latter banks would, in the long run, derive an advantage in the shape of an easy money-market in India from the institution of a State Bank which would far outweigh its possible disadvantages to them. As regards the other Banks—they would all gain so substantially by such a creation that we need apprehend no jealousy or opposition from that quarter. In support of this view we may cite the instance of the Bank of France which helps other banks by offering facilities for the rediscount of commercial paper in the hands of the other banks. We may conclude then, that though at first sight the proposal for an Imperial or State Bank in India is likely to be resisted by the Presidency and the Exchange Banks, a clearer realisation of the nature and scope of such a Bank, with all its advantages to the Banking institutions in general, would convince them of its benefits to the general money-market in India.

We cannot say the same thing about some other aspects of this proposal. If the new Bank is to be made a department of state we can hope for very limited gains from its institution. The management of such an institution would require an order of talent and a kind of training which the average public servant of the type that now directs the Indian Finance Department does not possess. Elsewhere we have mentioned some of the defects

which characterise even the ordinary private banker and financier in India. If the proposed State Bank is to be saved from the incompetence of the one or the weakness of the other, men of an altogether different type will have to be placed at the head of the institution. Even so the battle is half-won. The best man at the head of affairs would be able to show very poor results if his action is confined in advance by hide-bound regulations. Red-tapism—the eternal curse of almost all public departments—would then reign supreme, and the money-market of India,—and even of the world, instead of being a gainer would suffer exceedingly from the constant meddlesomeness of officials. This is a far greater danger than all the others put together. We do not, indeed, deny the need of sound regulations for the conduct of an Imperial Bank; but we think that such an institution would not achieve the success it deserves, if wide latitude—not incompatible with the general safety of the body—is not allowed to the Directors of such an institution for the exercise of their discretion in devising expedients for developing the business of the Bank.

Apart from the probable jealousy of the existing banks, and the possible incompetence of the chief officials with all its consequences of red-tapism, we need fear no great obstacle to the success of such a Bank. It is true that the variety of conditions which prevails in the different parts of India would demand varying treatment which the consti-

tution of such a Bank would not facilitate, or which the training and experience of its Directors would not be equal to. But this is a difficulty which may soon be overcome with a little experience. The constitution of the Bank, indeed, must leave a wide margin of powers to the authorities of the Bank to prevent red-tapism ruining the Bank, if not dislocating the whole money-market of India, as well as to facilitate the coping with each new emergency by new expedients.

#### IV. FUNCTIONS OF THE BANK.

We have now discussed the chief reasons for the institution of an Imperial Bank and some of the obstacles that might possibly arise in its way. Let us now discuss the functions which may safely be made over to this Bank. If we are right in our conclusions that the basic principles of the note-issue of India need a thorough revision, we may consider the management of the Paper Currency to be among the most important of the functions of such a Bank. Being in intimate daily touch with the business community all over India the proposed Bank would feel the need of an expansion in the currency long before it is perceived by any other body; and, if the law governing the paper currency permits it, it would try to meet this need the moment it is felt. In the same way it could and would deal with a redundancy of currency, and thus secure the benefits of an automatic currency which can always easily adjust itself exactly to the

needs of commerce. It may be urged that the Government also can do this if the fundamental principle of paper money be altered. But the Government is not—and cannot be—in intimate daily contact with the commercial community. By the time the Government realise the need for an expansion or contraction, and decide to take action the evil would, in all probability, have already been done. And the action of the Government will always lack that silent self-acting smoothness, which is the essence of all such operations and which a State Bank would accomplish a marvel.

If the Bank is a Government Bank it would be allowed almost as a matter of course—to receive all Government dues and pay all Government demands free of charge. The trouble of keeping accounts may be assumed to be adequately compensated for by the considerable public balances which would always remain with the Bank, and on which the Government would not charge any interest. So also with regard to the management of our public debt. The public debt of the Government of India is too large, too complex not to require expert handling. To make it over to this Bank would be a gain both to the State and to the Bank. But we cannot expect—in reason and in justice—the Bank to discharge this function and to accept the heavy responsibilities connected with it gratis. The Bank of England is remunerated for similar services at the rate of £ 325 a year on every million pounds up



to £ 500,000,000 and £ 100 a year for every million in excess of this sum. We may assume that when the Bank is started after the war-if at all it is started-the Bank could not go on discharging that function without any remuneration.

The proposed Bank might also very well take up the Exchange business on account of the Government. In itself this would be a considerable item if the Bank confined itself exclusively to the Exchange business on account of the State; but there is no reason why the Bank should be prevented from dealing in Exchange in general. At the present time it would also mean the maintenance of the Exchange value of the rupee. This would be as important a function as that of managing the Paper Currency so long as this artificial system of currency is retained. We have opposed this system too definitely in this book to desire its continuance even in the hands of such an institution, though we must admit that the Imperial Bank would be a far better body to manage our artificial gold exchange standard than a body of ordinary public servants. And when the present system is abolished and a Gold Standard substituted, we may still allow the Imperial Bank to buy bullion on account of the Government.

There is a substantial agreement on all these points among writers on this subject. But on two points-the management of the Mint and of the Gold Standard Reserve-there seems to be some difference of opinion. As regards the latter the situation is

inevitable, though deplorable, so long as the present currency policy is pursued. And if we have a Gold Standard with a Gold Currency, we would need such portion of this reserve as is not used for the purpose of introducing a Gold Currency, to combine with the Paper Currency Reserve and form one great Reserve to serve both Currency and banking purposes. Under the existing circumstances the question may well be debated as to which authority should manage this Reserve, the proposed Bank or the Government. If this Reserve is ever at all to be used for banking purposes it had best be left with the Bank. On the other hand if it is to be purely and simply a currency Reserve it would be better if the Government had its exclusive management, since the credit of the Government is too intimately involved in the maintenance of the exchange value of the Rupee, to permit them to take any risks in the matter. The original purpose of the Reserve was, not indeed, to serve exclusively the purpose of maintaining the exchange value of the rupee, but in course of time it has been often used in a manner to suggest its close affinity, if not identity with, a Banking Reserve. Even so to leave that reserve with a Bank, however sound, would be to court risks. We think, therefore, that whatever the ultimate purpose of the Gold Standard Reserve may be, so long as the exchange value of the rupee needs delicate handling, the Reserve should be held and managed by the Government. And as regards the Mint, also, though the need for coining

just that quantity of rupees which experience tells us would be required, is very urgent and though that need can be slightly estimated only by a Bank, the necessity to maintain the purity of the currency imperatively demands that the management of the Mint should be a public concern. The Mint and the Bank would, no doubt, have to be in very close connection, but if such a close connection can be secured without an identity of management it would always be preferable to do so.

#### V. ADVANTAGES OF THE INSTITUTION.

Having examined the functions of such a Bank let us now discuss the advantages of the proposal. The reasons we have given above point sufficiently clearly to the principal advantages of such a proposal. The Bank, if established, might be instrumental in bringing about a more popular and elastic note-issue, as well as considerable ease in the Indian money-market which is liable to almost regularly periodic stringency. The wide fluctuations in the Indian Bank rate from season to season will be diminished by a more complete co-ordination between the demands of the business world and those of the Government. And, if it is enjoined on the Bank that it should have branches in every important centre in India, banking would be considerably extended, the idle wealth of India—if any—would be drawn out to help commerce and industry and the Indian financial conditions would become more stable. We need hardly point out the im-



mense help that such a bank might be able to render to commerce industry and agriculture of this country.

The advantages to the State are no less obvious than to the public. With a more popular paper currency, more money would be economised for investment in Government paper, and so bring about a material advantage in the saving of interest. The existing system of independent Treasuries would then be not wanted, and the great waste which this system engenders will be avoided. But, above all, government officials will be relieved and the complicated questions of finance would be made over to persons who understand them.

We have intentionally refrained from discussing the constitution of such a Bank because, within the scope of this work, we cannot do justice to the various devices of founding and governing such an institution, all of which would combine in some measure state control, state aid, and general public confidence. The one principle, however, on which we would like to lay emphasis even in this little book, is that on no account should the proposed Bank be allowed to degenerate into a Government department. If the Bank is at all to be useful in solving the many and intricate problems of Indian Finance, it must not succumb to red-tapism, it must not ignore the value of public criticism and public confidence. The element of State control would, no doubt, be indispensable not only because of the immense privileges that would have to be given by



the Government to this Bank, but also to insure a vigilant care from entirely different points of view. To combine the principles of state control with the freedom of action by the Directors of the Bank is not easy, but at the same time not impossible. The extent of State control would naturally vary according as the state wholly or partly finds the capital for the Bank, or merely gives it its business with some additional privileges. At the risk of being paradoxical we would hazard the statement that the State should find the capital for the Bank as well as give its business to the Bank, and yet exercise only that degree of control which is essential in public interest, and which is not incompatible with the success of the Bank. It would lead us, however, too much into details to discuss how the capital should be found, managers appointed, rules of business framed. Suffice it for our purpose to repeat that the Bank would be founded in the interests both of the Government as well as of the business world; and that the constitution should be based on the lines which would make it of the maximum possible benefit both to the State and to the people.

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## APPENDIX A.

### **The Indian Currency Act ( Draft ).**

AN ACT ( DRAFT ) TO CONSOLIDATE AND AMEND  
THE LAW RELATING TO GOLD, SILVER,  
BRONZE AND NICKEL COINAGE, PAPER  
CURRENCY AND THE MINT IN INDIA.

Whereas it is expedient to consolidate and amend the law relating to gold, silver bronze and nickel coinage, paper currency and the Mint in India ; it is hereby enacted as follows :—

1. This Act may be called the Indian Currency  
**Short title and extent.** Act of—, and it extends to the whole  
of British India inclusive of British  
Baluchistan, Santhal Parganas and the Pargana of  
Spiti, as well as such Native states as are declared  
by the Governor General in Council in the Gazette of  
India, under rules made by the Governor General  
in Council, to have consented to adopt the system  
established by this Act.\*

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\* The provision extending the operation of this Act to the Native states has been inserted with a view to render the currency system of the whole of India as uniform as possible. It is a point of detail, but still it is true, that the differences in local currencies in India cause immense hardship to the internal trade of India. Just as in the interests of the development of of internal trade the Government have tried to remove all customs barriers, so also it is high time these differences in currencies were removed. We are aware, of course, that this is a matter which can only be settled by diplomatic negotiations. It is not inconceivable that the states which still retain their

2. In this Act, unless there is any thing repugnant in the subject or context,  
**Definition:**

- (a) "Standard gold" or "standard silver" means gold or silver eleven-twelfths of which is pure metal and one-twelfth is alloy.
- (b) "Standard of currency" means the gold coin of 96 grains troy, 88 grains of which is pure gold and 8 grains alloy.\*
- (c) "Standard weight" means the weight prescribed for any coin.

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own currencies should cling fondly to this one remnant of their former sovereign rights. But thanks to the growth of good sense amongst the rulers and their ministers, as also to the perception of the difficulties in the way of commerce caused by these barriers, we need not despair of arrangements being made to ensure a uniform currency organisation. Hence we reserve powers to the Governor General in Council to make rules granting adequate compensation to the states for the sacrifice of this right, or arranging for fixed rates of exchange between the British and the local state currency, provided the material is the same. after consultation with the states concerned. And on these rules being accepted the Indian Currency system may, by notification in the Gazette of India, be extended to the Native States in question.

\* We have adopted 96 grains as the weight of our standard of currency in the belief that such a coin would be neither too small nor too large for our purposes. It is better than the English sovereign of 123 odd grains, which might prove too large, and also than the German mark of 6 grains of which an actual coin would be too small to be useful. Besides, such a coin would have a distinctive Indian appearance and for that reason, too, it would be preferred.

- (d) "Deface" with its grammatical variations and cognate expressions includes dipping, filing, stamping, or such other alteration of the surface or shape of a coin as is readily distinguishable from the effects of reasonable wear;
- (e) "The Mint" includes the mints now existing and any which may hereafter be established.
- (f) "Prescribed" includes prescribed by a rule made under this Act.
- (g) "Remedy" means variation from the standard weight and fineness.

3. The Governor-General in Council may, by  
**Power to** notification in the Gazette of India:—  
**establish and**  
**abolish mints.**

- (a) establish a mint at any place at which a mint does not for the time being exist; and
- (b) abolish any mint whether now existing or hereafter established.

## GOLD COINAGE.

4. (1) The following gold coins only shall be  
**Gold coins.** coined at the Mint for issue under  
the authority of the Governor-General in Council, namely:—



(a) A Mohar, the standard of currency,

(b) An "adhela" being half the weight of the Mohur.\*

(2) The standard weight of the Mohar shall be ninety-six grains Troy and its standard fineness† shall be as follows: namely, eleven-twelfths or eighty-eight grains of pure gold and one-twelfth or eight grains of alloy.

(b) The other gold coins shall be of proportionate weight and of the same fineness.

### SILVER COINAGE.

5. The following silver coins only shall be coined at the mint for issue under the authority of the Governor General in Council, namely:—

(a) a rupee to be called the Government rupee;

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\* Further subdivision of gold coins has been omitted, as smaller coins are very inconvenient to handle. Even the Adhela, if we may believe the authorities on the subject in England and elsewhere, would be too small to handle.

† We have kept unchanged the standard fineness, in order to avoid confusion or complication. When, however, the whole system is being recast it might well be considered whether we should not adopt the more scientific and simpler system of nine-tenths fineness. In that case it would be convenient to have the gold piece of 100 grains and the rupee of 200 grains. We might even introduce with advantage the gram instead of the Troy grain as the unit of weight.

(b) a half rupee or eight anna piece ;

(c) a quarter-rupee, or four annas piece; and

(d) an eighth of a rupee, or two anna piece.

6. (1) The standard weight of the Government rupee shall be one hundred and eighty grains Troy, and its standard fineness shall be as follows, namely: eleven-twelfths or one hundred and sixty-five grains of fine silver and one-twelfth or fifteen grains of alloy.

(2) The other silver coins shall be of proportionate weight and of the same fineness.

7. The Mohar shall be taken as equivalent to ten Government rupees, and the subdivision of the Mohur and rupee shall be taken as equivalent in like proportions.

8. In the making of gold and silver coins a  
 Remedy. remedy shall be allowed of an  
 amount not exceeding the following  
 namely :—

	Remedy in weight.	Remedy in fineness.
Mohur ...	} Five thousandths..	Two thou- sandths.
Rupee half- rupee ...		Two thou- sandths.
Quarter rupee.	Seven thousandths.	} Three thou- sandths.
Eighthth rupee.	Ten thousandths ...	

## NICKEL COINAGE.

9. The following nickel coin only shall be coined at the Mint for issue under the authority of the Governor-General in Council, namely, a one-anna piece.

10. The standard weight of the one-anna piece shall be sixty grains troy; provided that in the making of nickel coin, a remedy shall be allowed of an amount not exceeding one-fortieth in weight.

## BRONZE COINAGE.

11. The following bronze coins only shall be coined at the mint for issue under the authority of the Governor-General in Council, namely.

- (a) A pice or quarter anna
- (b) A half-pice or one-eighth of an anna
- (c) A pie or one-third of a pice.

12. (1) The standard weight of the pice shall be 75 grains troy and the other bronze coins shall be of proportionate weight.
- (2) Bronze coins shall be coined from a mixed metal consisting of copper, tin and zink.

Provided that in the making of bronze coins, a remedy shall be allowed not exceeding one-fortieth in the weight.

## DIMENSIONS AND DESIGNS OF COINS.

13. (1) The Governor General in council, by notification in the gazette of India, may
- (a) direct the coining and issuing of all coins, referred to in the several preceding sections, and
  - (b) determine the dimensions of, and designs for, such coins.
- (2) Until the Governor General in Council<sup>1</sup> otherwise determines by notification under sub-section (1), the dimensions and designs of the silver coins coined under this act shall be those prescribed for the like silver coins under the Indian coinage Act, 1870, at the time of the commencement of this Act.
- (3) The dimensions of the Mohur shall be 25 millimetres in diameter and 2 millimetres in thickness. The design on the Mohur shall be the arms of the Government of India on the reverse, with the year when the coin was struck, and the impression of the king-emperor's likeness, with his name and title on the obverse.

### LEGAL TENDER.

14. The gold coins, viz. Mohur, and Adhela shall be a legal tender in payment or on account : provided that the coin,



(a) has not lost in weight so as to be more than one per cent below standard weight, and

(b) has not been defaced.

15. Gold coins whether coined at His Majesty's Royal mint in England or at any mint established in pursuance of a proclamation of His Majesty as a branch of the Royal Mint, shall not be a legal tender in payment or on account.\*

16. (1) The silver coins, namely the rupee and half-rupee, shall be a legal tender in payment or on account for sums not exceeding fifty rupees at one time provided that the coin

(a) has not lost in weight so as to be more than two per cent below standard weight, and

(b) has not been defaced.

(2) The quarter-rupee and eighth of a rupee shall be a legal tender in payment or

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\* With the overhauling of the whole coinage system the question of legal tender must be reconsidered. If a gold coin is introduced the rupee must of necessity become a limited legal tender; and considering the extent of monetary transactions in India, the limit of Rs. 50 is sufficiently high to keep a considerable stock of rupees in circulation and thus economise the use of gold. The discontinuance of the legal tender of English gold coins is inserted for the sake of simplicity. They may, however, be received at their intrinsic gold value. The legal tender of the smaller silver coins has been raised, but that of the nickel and bronze coins has been kept at its original level.

on account for any sum not exceeding two rupees provided that the coin

- (a) has not lost in weight so as to be more than such percentage below standard weight as may be prescribed as the limit of reasonable wear, and
- (b) has not been defaced.

17. The Nickel coin specified in section shall be a legal tender in payment or on account for any sum not exceeding one-rupee at the rate of sixteen for a rupee.

18. The bronze coins specified in section shall be a legal tender for payment or on account for any sum not exceeding one rupee at the following rates respectively, namely:—

- (a) the pice at the rate of 64 for a rupee
- (b) the half piece at the rate of 128 for a rupee
- (c) the pie at the rate of 192 for a rupee.

18. All silver and copper coins issued under the Acts XVII and XXI of 1835, XXI of 1838, XXII of 1844, XIII of 1862 and the Indian Coinage Act of 1870, and declared by those Acts to be legal tender shall continue to be legal tender in the manner specified in Ss. 16 and 18 of this Act, provided that the Governor-General in council may, by proclamation in the Gazette of India, declare those coins to

be no legal tender after a specified date, before which they may be received at the mint to be converted into an equal number of the like new coins issued under this Act.\*

20. The Mint shall be open to the Public for the coinage of gold coins free of charge. †

21. †The Mint shall receive gold bullion to be coined at the rate of 5 gold Mohurs for one ounce of gold of standard fineness.

22. The Mint shall not be open to the public for the coinage of any coins other than the gold coins.

### THE PROFIT

23. The profits of coinage shall be applied in the following order, namely.

(a) to the upkeep of the Mint establishment;

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\* This provision is inserted to replace gradually the old and worn out coins in circulation by new ones.

† This provision is inserted as a free mint for the coinage of gold is a necessary accompaniment of a gold standard and a gold currency. The rate at which the gold bullion should be receivable at the Mint to be coined is fixed for standard gold *i. e.* eleven twelfths fine. For pure gold it would be  $\frac{18}{8}^0$ . Mohurs 5.45 or 5 M. 4 Rs. 8  $\frac{8}{11}$  annas. The rupee being reduced to the position of token its coinage must be monopolised by the State and the Mint must remain closed to the public for its coinage, as also for the coinage of the subsidiary tokens.

- (b) to the purchase of gold bullion for coinage purposes not exceeding one third of the remainder.
- (c) to the purchase of silver and other metals for purposes of coinage, if any be required.\*
- (d) to a Reserve Fund which shall be used to support the Paper Currency in case of an unexpected, heavy, demand for conversion.

#### DIMINISHED, DEFACED AND COUNTER- FEIT COINS.

24. Where any gold or silver coin, which has been coined and issued under this Act, is tendered to any person authorised by the Governor-General-in-Council or by the local government to act under this section, and such person has reason to believe that the coin

- (a) has been diminished in weight so as to be more than such percentage below standard weight as may be prescribed as the limit of reasonable wear, or

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\* The reasons for these provisions are obvious. The purchase of gold for purposes of coinage out of the profits of token coinage was meant by the Fowler Committee to facilitate the introduction of a gold currency. The purchase of silver is also not a new provision; and the use of the fund for meeting paper currency demand is suggested by the later day practice, and justifiable on the ground of the unexpectedness of the demand.



- (b) has been defaced,  
he shall, by himself or another cut or  
break the coin.

25. A person cutting or breaking a coin under the provision of clause (a) of section 24 shall observe the following procedure, namely—

- (a) If the coin has been diminished in weight so as to be more than such percentage below standard weight as may be prescribed as the limit of reasonable wear, but not more than such further percentage in this behalf, he shall either return the pieces to the person tendering the coin, or, if such person so requests, shall receive and pay for the coin at such rates as may be prescribed in this behalf; and

- (b) If the coin has been diminished in weight so as to be more than such further percentage below standard weight so prescribed as aforesaid, he shall return the pieces to the person tendering the coin, who shall bear the loss caused by such cutting or breaking

26. A person cutting or breaking a coin under the provisions of clause (b) section 24 shall observe the following procedure, namely—

- (a) If such person has reason to believe that the coin has been fraudulently

defaced, he shall return the pieces to the person tendering the coin, who shall bear the loss caused by such cutting or breaking ;

- (*b*) If such person has not reason to believe that the coin has been fraudulently defaced, he shall receive and pay for the coin at its nominal value.

27. If a coin is liable to be cut or broken under the provisions of both clause (*a*) and (*b*) of section 24 of this Act, the person cutting or breaking the coin shall deal with it,—

- (*a*) if he has reason to believe that the coin has been fraudulently defaced, under clause (*a*) of section (26) and

- (*b*) in other cases, under section 25.

28. Where any gold or silver coin, purporting to be coined or issued under the authority of this Act, is tendered to any person authorised by the Governor-General in Council or by local Government to act under this section, and such person has reason to believe that the coin is counterfeit, he shall, by himself or another, cut or break the coin, and may, at his discretion, either return the pieces to the tenderer who shall bear the loss caused by such cutting or breaking, or receive and pay for the coin according to the value of the bullion contained in it.

## SUPPLEMENTAL PROVISIONS.

29. (1) The Governor General in council may make rules to carry out the purposes and objects of this Act

(2) In particular, and without prejudice to the generality of the foregoing part, such rules may—

(a) reduce the amount of remedy allowed by any of the preceding sections in the case of any coin;

(b) provide for the guidance of persons authorised to cut or break coins under Ss. 24 and 28;

(c) determine the percentage of diminution in weight below standard weight, not being less in any case than 2 per cent which shall be the limit of reasonable wear;

(d) prescribe the further percentage referred to in clause (a) of section 25 and the rates at which payments shall be made in the case of coins falling under the same clause; and

(3) Every such rule shall be published in the gazette of India, and all such publication shall have effect as if enacted in this Act.

30. No suit or other proceeding shall lie against any person in respect of anything in good faith done or intended to be done, under or in pursuance of the provisions of this Act.

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## PART II.

### Paper Currency.

31. "Universal Currency Note" means a note of the donominational value, of two, five, ten and fifty mohurs, or a note of any other denominational value which the Governor-General in Council may, by notification in the Gazette of India, declare to be a universal Currency Note.

32. At the head of the Department shall be an officer to be called the Head Commissioner of Paper Currency.

33. The Governor-General in Council may, by notification in the Gazette of India:—

(a) establish districts to be called circles of issue, seven of which circles shall include the towns of Calcutta, Madras, Bombay, Rangoon, Lahore, Cawnpore and Karachi, respectively,\*

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\* The system of separate circles, though it has been adversely criticised on the ground that it prevents the popularisation of notes, has, however been retained in this draft, because to do away with it altogether would be to incur too large a responsibility. By increasing the denomination of the Universal Currency note we have taken the sting out of the above criticism. And should the experiment succeed there would be only a small act needed to do away with separate circles. Besides, in a subsequent section provision is made for greater facilities of encashment.



- (b) appoint in each circle some one town to be the place of issue of currency notes as hereinafter provided,
- (c) establish in each such town an office or offices of issue:—and
- (d) establish in any town situate in any-circle an office to be called a currency office

33. There shall be a department of Public Service, to be called the department of Paper Currency, whose function shall be the issue of Promissory notes of the Government of India, to be called Currency Notes, payable on demand, and of such denominational value, not less than two Mohurs, as the Governor-General may direct.

- 34. (1) The Head Commissioner of Paper Currency shall be the officer in charge of the circle of issue which includes the town of Calcutta.
- (2) For each other circle of issue there shall be an officer in charge to be called the Commissioner of Paper Currency, and for each Currency Agency an officer to be called the Currency Agent.

35. For the purposes of this Act

- (a) Commissioners of Paper Currency shall be subordinate to the Head Commissioner of Paper Currency and
- (b) the Currency Agent at any town shall be subordinate to the Head Commissioner or Commissioner, as the case may be, of Paper Currency for the circle of issue in which that town is situate.

36. All officers under this Act shall be appointed by the Governor-General in Council.

37. (1) The Head Commissioner of Paper Currency shall provide currency notes of the denominational values prescribed under this act, and shall supply the Commissioners and Currency Agents subordinate to him with such notes as they need for the purposes of this Act.

(2) The Commissioners shall supply the Currency Agents subordinate to them, respectively, with such notes as these agents need for the purposes of this Act.

(3) Every such note, other than a Universal Currency note, shall bear upon it the name of the town from which it is issued.

38. The name of the Head Commissioner, of one of the Commissioners, or of some other person authorised by the Head Commissioner, or by one of the

Commissioners to sign Currency Notes, shall be subscribed to every such note, and may be impressed thereon by machinery, and when so impressed shall be deemed to be a valid signature.

39. The officers in charge of circles of issue shall, in their respective circles, on the demand of any person, issue, from the office or offices of issue established in their respective circles, currency notes of the denominational values prescribed under this Act, in exchange for the amounts thereof

(a) in gold coin of India issued under, and made legal tender by, this Act, or gold bullion.

(b) In rupees to the extent of not exceeding fifty.\*

40. Any currency Agent to whom currency notes have been supplied under section 37 of this Act may, if he thinks fit, on the demand of any person, issue from his agency any such notes in exchange for the amount thereof in coin or bullion as prescribed by section 39 of this Act.

41. If the Government of India consents to hold in gold coin or bullion, or in securities of the kinds

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\* This last provision is inserted to allow the notes to displace the rupees from circulation as much as gold. Strictly speaking the provision would be illogical according to the general principle underlying this Act, but it is a concession-as reasonable as it is necessary, to the advocates of a scientific currency, which would economise to the utmost possible extent the use of precious metals.

mentioned hereafter, the equivalent in value to notes issued in India, as a reserve to secure the payment of these notes, the Governor-General in Council may from time to time direct that currency notes shall be issued to an amount equal to the value of the coin, bullion, and securities so held by the Government of India.\*

### CURRENCY NOTES WHERE LEGAL TENDER AND PAYABLE.

† 41. A Universal Currency Note shall be a legal tender at any place in British India for all purposes for the amount expressed in the note in payment or on account.

42. Any other Currency Note shall be a legal tender at any place in British India for the amount expressed in the note in payment or on account of any revenue due to the Government of India, or of any charges of the state or guaranteed railways in

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\* We have dropped from this section the alternative of holding a part of the reserve in silver bullion as it would be contrary to demonetisation of silver advocated by this Act. Besides there would be no need to keep a silver reserve, since the notes are redeemable in gold, though for convenience', sake we have introduced a permissive clause for redemption upto fifty rupees in silver.

† These three sections are changed considerably with a view to make the note circulation as wide and popular as possible. To this end we have (1) increased the denomination of the universal Currency Notes and (2) placed all other notes on the same footing as the universal currency note for the purposes of payment to Government or Railway or other public bodies.



India, or any other public corporation working under the control of the Government in India.

43. Any Currency note, other than a universal Currency note, shall be a legal tender at any place within the circle from which the note was issued, for all purposes of payment or on account.

44. No currency note shall be deemed to be a legal tender by the Government of India at any office of issue.

45. A currency note shall be payable at the following offices of issue, namely;—

(a) a universal currency note at any office of issue,

(b) any other note at any office of issue within the circle in which it was issued, or,

(c) under regulations made by the Government of India in that behalf, at the head office or any specified branch of the Presidency Banks of Bengal, Madras or Bombay.

46. For the purposes of sections 44 and 45 of this Act currency notes issued from any currency agency shall be deemed to have been issued from the town appointed under section to be the place of issue in the circle of issue in which that agency is established.

47. Where an office of issue is closed, the Governor-General in Council shall, by notification in the Gazette of India, direct that, with effect from the date of the closing of such office, all currency notes issued therefrom shall, for purposes of sections 44 and 45 of this Act, be deemed to have been issued from such other office as may have been specified in such notification.

### RESERVE.

48. The whole amount of currency notes at any time in circulation shall not exceed the total amount represented by gold coin and bullion, and the sum expended in the purchase of securities, which are held by the Government of India as a reserve to provide for the satisfaction and discharge of the said notes, and the said notes shall be deemed to have been issued on the credit of the Government of India as well as on the security of the said gold coin and bullion and securities.

Provided that for the purposes of this section, currency notes which have not been presented for payment, in the case of notes of any denominational value not exceeding ten mohurs within forty years, and in the case of notes of any denominational value exceeding ten mohurs within one hundred years, from the first day of April following the date of their issue, shall be deemed not to be in circulation.

Provided further that all notes which are declared under the first proviso to this section not to be in circulation, shall be deemed to have been issued on the credit of the Government of India and shall, if subsequently presented for payment, be paid from the revenues of the Government of India.

49. The securities mentioned in the next preceding section shall be securities of the Government of India, or securities issued by the Secretary of State for India in Council under the authority of an Act of Parliament and charged on the revenues of India, or securities of the United Kingdom of Great Britain and Ireland. Provided that the securities of the United Kingdom of Great Britain and Ireland shall not exceed at any time one-fourth of the total securities held in the Reserve, and that they shall not be purchased except when the net return from them is greater in proportion than from the securities of the Government of India.\*

† 50. The value of all the securities at the price at which they are purchased shall not exceed two crores of Mohurs so long as the total value of notes in circulation does not exceed six crores of Mohurs.

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\* We have already explained our reasons why we think the entire Reserve should be held in India, and why the securities should be preponderantly the securities of the Government of India.

† These two sections are an attempt to effect a compromise between the rival principles of a Proportional Reserve and a Fixed Reserve.

51. When the total value of the notes in circulation exceeds six crores of Mohurs, the securities in the Reserve may be increased in the proportion of one half of the excess circulation at the most.

52. If any coin or bullion held by the Secretary of State for India in Council is transmitted to the Governor General in Council, it shall be deemed during the period of transmission to remain part of the Reserve.

53. The securities purchased by the Governor General in Council shall be securities of the Government of India, and shall be held by the Head Commissioner and the Master of the Mint at Calcutta, or of such other mint as the Governor General in Council may direct in this behalf, in trust for the Government of India.

54. (1) The Head Commissioner may, at any time, when ordered so to do by the Governor General in Council, sell and dispose of any of the securities held under the next preceding section.

(2) For the purpose of affecting such sales the Master of the Mint at Calcutta, or of such other mint as aforesaid, shall, on a request in writing from the Head Commissioner, at all times sign and endorse the securities and the Head Commissioner, if so directed by the Governor General in Council, may purchase securities of the Government of India to replace such sales.



55. An account showing the amount of interest accruing on the securities held as part of the Reserve under this Act, and the expenses and charges incidental thereto, shall be rendered annually by the Head commissioner to the Governor General in Council, and published annually in the Gazette of India.

56. No person or corporation in British India shall draw, accept, make or issue any bill of exchange, hundi, promissory note, or engagement for the payment of money payable to bearer on demand, or borrow, owe or take up any sum or sums of money on the bills, hundies, or notes payable to bearer on demand of any such person.\*

Provided that cheques or drafts payable to bearer on demand or otherwise, may be drawn on bankers, shroffs or agents by their customers or constituents in respect of deposits of money in the hands of those bankers, shroffs or agents and held by them at the credit and disposal of the persons drawing such cheques or drafts.

57. Any person contravening the provisions of the next preceding section shall, on conviction by a Presidency Magistrate or a Magistrate of the First Class, be punishable with a fine equal to the amount of the bill, hundi, note or engagement in respect whereof the offence is committed.

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\* These provisions establish the monopoly of note issue in the Government of India.

58. An abstract of the accounts of the department of Paper Currency showing—

- (a) the whole amount of the currency notes in circulation
- (b) the amount of coin and bullion reserve, distinguishing gold from silver, and showing separately the amount held by the Secretary of State for India in Council or in transit or in the custody of a Mint Master during coinage
- (c) the nominal value of, and the price paid for, the securities held as part of the Reserve, showing separately the securities of the Government of India and those of the United Kingdom of Great Britain and Ireland,

shall be made up four times in each month by the Head Commissioner, and published as soon as may be, in the Gazette of India.

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**APPENDIX B.**  
**BANK OF ENGLAND.**  
**ISSUE DEPARTMENT.**

	For week ending 15-7-1914.	For week ending 1-8-1917.
Notes Issued	£ 56,908,235	£ 11,015,100
...		7,434,900
		38,458,235
		.....
	56,908,235	56,908,235
		68,295,650
		.....
		68,295,650

**BANKING DEPARTMENT.**

	For week ending 15-7-1914.	For week ending 1-8-1917.
Proprietors' Capital	£ 14,553,000	£ 50,439,661
Rest	3,431,484	110,654,852
Public Deposits*	13,318,714	27,592,980
Other Deposits	42,485,605	1,596,419
Seven-day and other Bills	29,010	16,167
	73,817,813	73,817,813
		191,524,106

\* Including Exchequer, Savings Banks, Commissioners of National Debt and Dividend Accounts.

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